

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-KSB** *ARL*



☒ **ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

For the fiscal year ended June 30, 2004

☐ **TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No. 1-13919



04051830

**Xponential, Inc.**

(Name of small business issuer in its charter)

**Delaware**

(State or other jurisdiction of incorporation or  
organization)

**75-2520896**

(I.R.S. Employer Identification No.)

**6400 Atlantic Boulevard, Suite 190**

**Norcross, Georgia**

(Address of principal executive offices)

**30071**

(Zip Code)

**PROCESSED**

Issuer's telephone number, including area code: **(678) 720-0660**

**DEC 13 2004**

Securities registered pursuant to Section 12(b) of the Exchange Act:

**THOMSON  
FINANCIAL**

Title of each class

Name of each exchange on which registered

**Common Stock, Par Value \$0.01 Per Share**

**OTC BB**

Securities registered pursuant to Section 12(g) of the Act: **None**

Check whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Check if there is no disclosure of delinquent filers pursuant to Item 405 of Regulation S-B is not contained in this Form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. ☐

State the issuer's revenue for its most recent fiscal year: **\$20,534,000.**

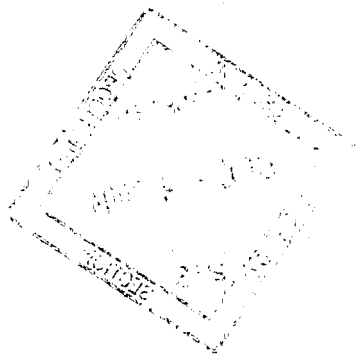
As of June 30, 2004 2,344,206 shares of \$0.01 par value common stock were issued and outstanding. The aggregate market value of the common stock held by non-affiliates, based on the book value of the common stock, was approximately \$3,829,000.

Check whether the issuer filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Exchange Act after distribution of securities under a plan confirmed by a court. Yes ☒ No ☐

**DOCUMENTS INCORPORATED BY REFERENCE**

None.

Transitional Small Business Disclosure Format (Check one): Yes ☐ No ☒



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**Xponential, Inc.**  
**Form 10-KSB Annual Report**  
**For the Fiscal Year Ended June 30, 2004**

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## PART I

### ITEM 1. DESCRIPTION OF BUSINESS

#### THE COMPANY

Xponential, Inc. (the "Company") was incorporated under the laws of the State of Delaware on January 13, 1994 and began operations under the name "Pawnco, Inc." On June 14, 1994 the Company changed its name to PCI Capital Corporation. On October 21, 1997 the Company changed its name to "PawnMart, Inc." On February 28, 2003 the Company changed its name to Xponential, Inc.

The Company is primarily a specialty finance and retail enterprise principally engaged in establishing and operating stores which advance money secured by the pledge of tangible personal property and sell pre-owned merchandise to value-conscious consumers. The Company operates 26 stores, commonly known as "pawnshops," through PawnMart, Inc., its wholly owned subsidiary. PawnMart generates income in two ways: through collection of a monthly service charge from advancing money to individuals based primarily upon the estimated resale value of pledged personal property such as jewelry, consumer electronics, tools, musical instruments, automobiles and other miscellaneous items and through profit realized on the retail sale of the unredeemed or other purchased pre-owned merchandise. The Company's principal office is located at 6400 Atlantic Boulevard, Suite 190, Norcross, Georgia and its telephone number is (678) 720-0660.

On July 9, 2001 the Company filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Northern District of Texas, Fort Worth Division (the "Bankruptcy Court") in the case of *PawnMart, Inc., Debtor*, Case No. 01-44957-BJH-11. The Plan of Reorganization was filed on February 15, 2002 and was amended on April 3, 2002 (the "Plan"). A confirmation hearing for the Plan was held on May 20, 2002 (the "Confirmation Date") and the Plan was confirmed by order of the Bankruptcy Court as of that date ("Confirmation Order"). The Plan became effective on May 31, 2002 (the "Effective Date"). Pursuant to the Plan, the Company merged with C/M Holdings, Inc., a Texas corporation ("CMHI"), on August 30, 2002 (the "Merger"), with the Company as the surviving entity. CMHI was an affiliate of Jeffrey A. Cummer and Dwayne A. Moyers, officers and directors of the Company.

In May 2002 the Board of Directors of the Company determined that it was in the Company's best interest to change its fiscal year end from the Saturday nearest January 31 to June 30 to more accurately reflect the Company's post-bankruptcy operating results. A transition report was filed for the five month period ended June 30, 2002 reflecting the change in the year end. "Fiscal 2004" is defined as the twelve month period ended June 30, 2004; "Fiscal 2003" is defined as the twelve month period ended June 30, 2003; "Fiscal 2002" represents the five month transition period ended June 30, 2002; and "Fiscal 2001" represents the 52 week period ended February 2, 2002.

#### INDUSTRY

Pawnshops provide short-term secured loans. Most pawn loans are for less than \$500. Industry sources believe that banks could not recover the administrative costs of these small loans without substantial increases in rates and charges. In addition, many pawn loans are made to people who would not qualify as "creditworthy" at a bank. An estimated 20 to 40 million people occasionally have short-term needs, such as for utility bills and medical expenses. For these people, pawnshops supply cash conveniently and quickly. The Company believes that pawnshops generally perform well during recessions and all other economic cycles due to (i) the need for loans by non-banking individuals remaining stable during such economic cycles and (ii) pawnshops serving as a value-priced retailer regardless of economic conditions.

## **BUSINESS STRATEGY**

The Company's primary business plan is to expand its existing pawnshop operation through internal growth of existing locations and selective acquisition of existing stores in the markets in which it currently operates. Management has determined that due to the rapid expansion the industry experienced in the late 1990s, attempting to open new locations at this time is not the most profitable strategy for expansion. Management intends to focus on acquiring existing pawn stores in its existing markets during the next fiscal year to increase the economies of scale of its current management structure which will improve short- and long-term profitability. Management has determined that because existing stores have an established customer base, pawn portfolio, and retail sales business, acquisitions will contribute more quickly to revenues and profitability than opening new locations. The Company acquired one store in the Atlanta metroplex and closed its only location in South Carolina during Fiscal 2004.

The Company also invests in and is seeking to acquire companies in the finance, retail or manufacturing industries where its management expertise in restructuring and expanding existing operations for companies with an established market can create additional value for its stockholders. The first such investment by the Company is American IronHorse Motorcycle Company, Inc. ("American IronHorse"), a specialty motorcycle manufacturer, which the Company invested in and has provided advisory services to since October 2003. As of June 30, 2004 the Company had invested \$3,018,000 in American IronHorse. The Company invested an additional \$1,395,000 to purchase additional equity in American IronHorse subsequent to June 30, 2004 and may increase its investments in American IronHorse in the future pending approval by the Company's Board of Directors.

## **ACQUISITIONS**

Because of the highly fragmented nature of the pawn industry, the Company believes that sole proprietors owning one or a few stores will be willing to sell suitable stores in the Company's target markets on terms that are favorable to the Company. Before making an acquisition, management studies demographic and traffic data for the surrounding area, the surrounding competition, and local regulatory issues that will affect the future success of the store operating under the Company's guidelines and market focus. Management considers the location of the store, the size and quality of the leased premises, the volume, quality and redemption history of outstanding pawn receivables and the quality and mix of inventory on hand in determining the price and desirability of stores considered for acquisition.

For businesses considered as acquisition candidates that are not pawn stores, management has determined that it will seek opportunities that are compatible with the consumer finance and retail operations it currently operates or will provide opportunities for value enhancement based on management's abilities to reorganize, restructure or expand capital constrained businesses that have a defined market or product niche.

## **CONTINUING STORE OPERATIONS**

The Company defines each of its stores as operating segments. However, management has determined that all of its stores have similar economic characteristics and also meet the other criteria which permit the stores to be aggregated into one reportable segment. The following discusses various aspects of the Company's store operations.

### *Lending*

The Company's pawn loans are secured by pledged tangible personal property which is intended to provide security to the Company for the repayment of the amount advanced plus accrued pawn service charges. Pawn loans are made without personal liability to the borrower. Collateral for the Company's

pawn loans consists of tangible personal property, generally jewelry, consumer electronics, tools, and musical instruments. The Company does not investigate the creditworthiness of a borrower, but relies on the estimated resale value of the pledged property, the perceived probability of its redemption, and the estimated time required to sell the item as a basis for its credit decision. The amount that the Company is willing to lend generally ranges from 20% to 75% of the pledged property's estimated resale value depending on an evaluation of these factors. The sources for the Company's determination of the resale value of collateral include catalogues, blue books, newspaper advertisements, and previous sales of similar merchandise.

The Company contracts for a pawn service charge as compensation for the use of the funds advanced to cover such costs as storage, insurance, title investigation and other transaction costs. The statutory service charges on loans at the Company's stores range from 24% to 300% on an annualized basis depending upon individual state regulations and the amount of the pawn loan. Pawn service charges totaled \$6,605,000 for Fiscal 2004. As a percent of the Company's total revenues, pawn service charges contributed 32.2% to the Company's total revenues in Fiscal 2004 compared to 32.2%, 31.9% and 28.7% during Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively. Pawn service charges contributed to 70.9%, 61.6%, 61.9% and 68.7% of the Company's gross profit during Fiscal 2004, Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively. The Company's average pawn loan was \$121, \$127, \$110 and \$114 at June 30, 2004, June 30, 2003, June 30, 2002 and February 2, 2002, respectively.

The pledged property is held through the term of the transaction, which generally is one month with an automatic redemption period which varies by jurisdiction from ten to sixty days in the states where the Company currently operates, except for automobile title loans, where a shorter redemption period applies under state regulations. The loan may be extended or renewed prior to the end of the redemption period. In the event the borrower does not repay or extend the pawn loan by the end of the redemption period, the unredeemed collateral is forfeited to the Company and becomes merchandise available for sale.

Georgia pawn regulations allow the Company to advance funds secured by automobile titles. Approximately 10.2%, 6.4%, 6.7% and 6.7% of the Company's total revenues during Fiscal 2004, Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively, were related to pawn service charges generated from such advances. During the term of the title loan, the borrower is allowed to maintain possession of the collateral, although for loans in excess of \$5,000 the Company's policy is to take physical possession of the vehicle and secure it at one of its storage sites. In the event of default, the Company contracts to repossess the automobile and subsequently disposes of the automobile through its retail operations. Although the Company is exposed to the risk that it is unable to locate the collateral securing forfeited title loans, it has not historically experienced material adverse results from these instances. The Company's primarily internal growth strategy is to continue to expand the auto title loan portion of its business due to the relatively low default rates and high renewal and redemption rates.

The recovery of the amount advanced, as well as realization of a profit on the sale of merchandise, is dependent on the Company's initial assessment of the property's estimated resale value. Improper assessment of the resale value of the collateral in the lending function can result in reduced marketability of the property and resale of the merchandise for an amount less than the amount advanced. For example, unexpected technological changes could adversely impact the value of consumer electronic products and declines in gold and silver prices could reduce the resale value of jewelry items acquired in pawn transactions and could adversely affect the Company's ability to recover the carrying cost of the acquired collateral. However, historically, the Company has experienced profits from the sale of such merchandise.

### *Retail Sales*

The Company retails pre-owned products acquired either when a pawn loan is not repaid or from individual customers or other sources. Merchandise acquired through defaulted pawn loans is carried at the amount of the related pawn loan, exclusive of any uncollected pawn service charges. Management believes that this practice will decrease the likelihood that the Company will experience significant, unexpected inventory devaluations.

Merchandise sales contributed to 66.1%, 67.2%, 66.8% and 69.8% of the Company's total revenues during Fiscal 2004, Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively. Merchandise sales contributed to 25.4%, 37.1%, 35.5% and 27.7% of the Company's gross profit during Fiscal 2004, Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively. The Company realized gross profit margins on merchandise sales of 17.4%, 28.8%, 27.4% and 16.6% during Fiscal 2004, Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively. See "Item 6. Management's Discussion and Analysis or Plan of Operation" for a discussion of factors affecting the results of operations of the Company's retail sales.

The Company does not provide financing to purchasers of its merchandise nor does it provide warranties or refunds for merchandise sold at any of its locations.

Prospective purchasers may purchase an item on layaway, whereby the purchaser will typically put down a minimum of 20% of an item's purchase price as a layaway deposit. The Company will hold the item for a ninety-day period during which the customer is required to pay for the item in full. As of June 30, 2004 layaway deposits held by the Company totaled \$93,000.

The Company writes down to lower of cost or market its merchandise held for resale based upon management's evaluation of the marketability of the merchandise. Management's evaluation takes into consideration the age of slow moving merchandise on hand and markdowns necessary to liquidate slow moving merchandise.

### *Retail Store Management*

Each location has a store manager who typically supervises its personnel and assures that it is managed in accordance with Company guidelines and established policies and procedures. Each store manager reports to a district manager who will typically supervise up to nine stores. At June 30, 2004 the Company had established four operating districts, each of which was managed by a district manager.

## **COMPETITION**

The Company encounters significant competition in the operation of its business. In connection with lending operations, the Company competes with other pawnshops (owned by individuals and by large operators) and certain financial institutions, such as consumer finance companies, which generally lend on an unsecured as well as on a secured basis. The Company's competitors in connection with its retail sales include numerous retail and discount stores who have greater financial resources than the Company. These competitive conditions may adversely affect the Company's revenues, profitability and ability to expand.

The Company's stores are positioned similarly to national discount stores. They are attractive, clean, well-lit and conveniently located. Merchandise is displayed in an organized, easy-to-shop manner and the Company's stores do not retail handguns, sporting rifles or assault rifles.

## **OPERATING CONTROLS**

The Company has an organizational structure that management believes can support a larger operating base. The store locations are monitored on a daily basis from corporate headquarters through

a centralized online computer system. The Company has an internal audit staff that performs physical counts of merchandise inventory and pawn loan collateral at each of the Company's locations approximately every sixty days. Additionally, the internal audit staff assists the corporate headquarters in verifying that the Company's policies and procedures are consistently followed. Management believes the current operating and financial controls and computer systems are adequate for its current operating base.

## REGULATION

The Company's store operations are subject to extensive regulation, supervision and licensing under various federal, state and local statutes, ordinances and regulations. Set forth below is a summary of the state pawnshop regulations in those states of the Company's operating locations at the end of Fiscal 2004.

*Georgia Pawnshop Regulations.* Georgia state law requires pawnbrokers to maintain detailed permanent records concerning pawn transactions and to keep them available for inspection by duly authorized law enforcement authorities. The Georgia statute prohibits pawnbrokers from failing to make entries of material matters in their permanent records; making false entries in their records; falsifying, obliterating, destroying, or removing permanent records from their places of business; refusing to allow duly authorized law enforcement officers to inspect their records; failing to maintain records of each pawn transaction for at least four years; accepting a pledge or purchase from a person under the age of eighteen or who the pawnbroker knows is not the true owner of the property; purchasing or accepting a pledge of merchandise on which the serial number has been altered or obliterated; making any agreement requiring the personal liability of the pledgor or seller or waiving any of the provisions of the Georgia statute; or failing to return or replace pledged goods upon payment of the full amount due (unless the pledged goods have been taken into custody by a court or a law enforcement officer). In the event pledged goods are lost or damaged while in the possession of the pawnbroker, the pawnbroker must replace the lost or damaged goods with like kinds of merchandise. Under Georgia law, total interest and service charges may not, during each thirty-day period of the loan, exceed 25% of the principal amount advanced in the pawn transaction (except that after ninety days from the original date of the loan, the maximum rate declines to 12.5% for each subsequent thirty-day period). The statute provides that municipal and county authorities may license pawnbrokers, define their powers and privileges by ordinance, impose taxes upon them, revoke their licenses, and exercise such general supervision as will ensure fair dealing between the pawnbroker and his customers.

*North Carolina Pawnshop Regulations.* In North Carolina the Pawnbrokers Modernization Act of 1989 regulates the licensing, reporting and financial responsibility of pawnbrokers. Appropriate city and county governments must be petitioned in order to acquire a license. Once licensed, a pawnbroker must keep consecutively numbered records of each and every pawn transaction. No pawnbroker may receive an effective rate of interest in excess of 2% per month, except that the pawnbroker may charge additional fees up to 20% per month for services such as title investigation, insurance, storage, reporting fees, etc., so long as certain total dollar limits are not exceeded. Mobile homes, recreational vehicles, or motor vehicles other than a motorcycle may not be pledged.

*Other Regulatory Matters, Etc.* The Bank Secrecy Act authorizes the United States Department of the Treasury to require financial service providers to maintain records of transactions involving currency in an amount greater than \$10,000 or the purchase of monetary instruments for cash in amounts from \$3,000 to \$10,000. In general, every financial institution, including the Company, must report each deposit, withdrawal, exchange of currency or other payment or transfer, whether by, through or to the financial institution, that involves currency in an amount greater than \$10,000. In addition, multiple currency transactions must be treated as single transactions if the financial institution has knowledge

that the transactions are by, or on behalf of, any person and result in either cash in or cash out totaling more than \$10,000 during any one business day.

The Gramm-Leach-Bliley Act and its implementing federal regulations require the Company to generally protect the confidentiality of its customers' nonpublic personal information and to disclose to its customers its privacy policy and practices, including those regarding sharing the customers' nonpublic personal information with third parties. Such disclosure must be made to customers at the time the customer relationship is established, at least annually thereafter, and if there is a change in the Company's privacy policy.

Effective February 1, 2003 the Company changed its policy with regard to loans on firearms to eliminate that portion of its business due to the increasing demands of regulatory agencies on the resale of firearms. The Company sold firearms acquired through defaulted loans only to properly licensed resellers. Prior to the elimination of the practice of loaning on firearms, each store was required to comply with the Brady Handgun Violence Prevention Act (the "Brady Act"), which took effect on February 28, 1994. The Brady Act imposes a waiting period/background check in connection with the disposition of handguns by federally licensed firearms dealers. In addition, the Company must continue to comply with the longstanding regulations promulgated by the Department of the Treasury, Bureau of Alcohol, Tobacco and Firearms, which require each store dealing in guns to maintain a permanent written record of all receipts and dispositions of firearms. The Company does not currently sell handguns, assault rifles or sporting rifles to the public.

In addition to the state statutes and regulations described above, many of the Company's stores are subject to municipal ordinances, which may require local licenses or permits, additional zoning restrictions, and specified record-keeping procedures, among other things. Each of the Company's stores, voluntarily or pursuant to municipal ordinance, provides to the police department having jurisdiction copies of all daily transactions involving pawn loans and over-the-counter purchases. These daily transaction reports are designed to provide the local police with a detailed description of the goods involved including serial numbers, if any, and the name and address of the owner obtained from a valid identification card.

A copy of the transaction ticket is provided to local law enforcement agencies for processing by the National Crime Investigative Computer to determine rightful ownership. Goods which are either purchased or held to secure pawn loans and which are determined to belong to an owner other than the borrower or seller are subject to recovery by the rightful owner. However, the Company historically has not experienced a material number of claims of this sort, and the claims experienced have not had a material adverse effect on the Company's consolidated results of operations.

#### *Employees*

As of June 30, 2004 the Company had a total of 146 employees all of which are employed on a full-time basis. The Company maintains a performance-based compensation plan for all store employees, based on, among other factors, profitability and special promotional contests. None of the Company's employees are covered by collective bargaining agreements. The Company considers its employee relations to be satisfactory.

#### *Insurance*

Casualty insurance, including burglary coverage, is maintained for each of the Company's stores, and fidelity bond coverage is maintained on each of the Company's employees.

Management of the Company believes its operations are conducted in material compliance with all federal, state and local laws and ordinances applicable to its business. There can be no assurance that additional local, state or federal legislation will not be enacted or that existing laws and regulations will not be amended which could have a material adverse effect on the Company's consolidated operations and financial condition.

## ITEM 2. DESCRIPTION OF PROPERTY

The Company currently leases all of its locations with monthly rental payments ranging from \$2,500 to \$7,000 per location and having initial lease terms expiring from October 2004 through October 2010. Substantially all of the Company's leased locations include renewal options. The size of the leased store locations range from approximately 1,800 to 19,075 square feet. The Company leases all of these properties from unaffiliated third parties.

The following table sets forth the geographic markets served by the Company and the number of stores in each market as of June 30, 2004, June 30, 2003, and June 30, 2002:

	Number of Stores as of June 30, 2004	Number of Stores as of June 30, 2003	Number of Stores as of June 30, 2002
Georgia:			
Atlanta Metropolitan Area .....	20	19	16
Dalton .....	1	1	1
Rome .....	1	1	1
Calhoun .....	1	1	1
Total Georgia .....	23	22	19
North Carolina:			
Charlotte .....	3	3	3
Total North Carolina .....	3	3	3
South Carolina:			
Greenville Metropolitan Area .....	0	1	1
Total South Carolina .....	0	1	1
Total .....	26	26	23

The Company considers its equipment, furniture and fixtures and leased buildings to be in good condition. The Company's leases typically require the Company to pay all maintenance costs, insurance costs and property taxes. The Company is operating one of its locations with a month to month lease.

## ITEM 3. LEGAL PROCEEDINGS

The Company is from time to time a defendant (actual or threatened) in certain lawsuits and arbitration claims encountered in the ordinary course of business, the resolution of which, in the opinion of management, should not have a material adverse impact on the Company's financial position, results of operation, or cash flows.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

An annual meeting of the stockholders of the Company was held on April 23, 2004. At that meeting the following matters were submitted to a vote of the stockholders:

The holders of shares of Common Stock are entitled to elect three members of the Board of Directors of the Company. Management's three Common Stock nominees listed in the proxy statement pertaining to the meeting were elected directors for the ensuing year. Of the 1,114,243 shares of Common Stock present in person or presented by proxy at the meeting, the number of shares of

Common Stock voted for, and the number of shares of Common Stock as to which authority to vote in the election was withheld, were as follows with respect to each of the Common Stock nominees:

<u>Name</u>	<u>Shares Voted For Election</u>	<u>Shares as to Which Voting Authority Withheld</u>
James R. Richards .....	1,092,600	21,643
Robert W. Schleizer .....	1,092,600	21,643
Carroll Dawson .....	1,092,600	21,643

The holders of shares of Series B Preferred Stock are entitled to elect four members of the Board of Directors of the Company. Management's two Series B Preferred Stock nominees listed in the proxy statement pertaining to the meeting were elected directors for the ensuing year. At the time of the election there were two vacancies on the Board of Directors and the Nominating and Governance Committee was conducting a search for two qualified individuals to serve on the Board of Directors, but as of June 30, 2004 had not identified such individuals. J. Robert Collins was subsequently appointed on July 13, 2004 as a director to represent the holders of Series B Preferred Stock. The Nominating and Governance Committee anticipates that it will recommend to the Board of Directors additional candidates to fill the remaining vacancy in the near future. Of the 480,902 shares of Series B Preferred Stock present in person or presented by proxy at the meeting, the number of shares of Series B Preferred Stock voted for, and the number of shares of Series B Preferred Stock as to which authority to vote in the election was withheld, were as follows with respect to each of the Series B Preferred Stock nominees:

<u>Name</u>	<u>Shares Voted For Election</u>	<u>Shares as to Which Voting Authority Withheld</u>
Jeffrey A. Cummer .....	480,902	0
Dwayne A. Moyers .....	480,902	0

A proposal to ratify the appointment of Grant Thornton LLP as independent auditors of the Company for the year ended June 30, 2004 was approved. Of the 1,114,243 shares of Common Stock and 480,902 shares of Series B Preferred Stock (with each such share being entitled to 3.44 votes) present or represented by proxy at the meeting voting together as a single class, 2,732,216 shares were voted for the proposal, 596 shares were voted against the proposal, and 35,733 shares abstained from voting with respect to the proposal.

## **PART II**

### **ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS**

#### **Market Information**

Under the terms of the Plan the Company cancelled all equity interest of common and preferred shareholders and issued 2,079,948 shares of Common Stock to its unsecured creditors in exchange for indebtedness. As of September 22, 2004 there are 2,344,206 shares of Common Stock outstanding. As of September 22, 2004 there were approximately 610 stockholders of record of the Common Stock. Company's Common Stock is currently trading on the Nasdaq Bulletin Board under the symbol XPOI.

In connection with the Merger, the equity holders of CMHI received 1,071,636 shares of Series A Preferred Stock and 500,042 shares of Series B Preferred Stock. The Preferred Stock has a liquidation preference over the Common Stock and the Series B Preferred Stock is convertible into 1,720,130 shares of Common Stock.

## Dividends

There have been no cash dividends declared on the Common Stock during the past two fiscal years. Section 170 of the Delaware General Corporation Law (the "Delaware Law"), restricts the declaration and payment of dividends to be made only from surplus, as defined in and computed in accordance with Sections 154 and 244 of the Delaware Law, or if there is no surplus, out of net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year, provided that dividends cannot be declared or paid from net profits if there is a capital deficiency, as defined in the Delaware Law, that has not been cured.

In addition, the Company's credit facility with FCC, LLC contains covenants prohibiting the payment of dividends, without the prior written consent of the lender, on the Company's Common Stock.

## Securities Authorized for Issuance Under Equity Compensation Plans

For the Company's equity compensation plans, the following table shows, at the end of Fiscal 2004, (a) the number of securities to be issued upon the exercise of outstanding options, warrants and rights, (b) the weighted average exercise price of such options, warrants and rights, and (c) the number of securities remaining available for future issuance under the plans, excluding those issuable upon exercise of outstanding options, warrants and rights.

### Equity Compensation Plan Information

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders . .	206,000	\$1.09	504,742(1)
Equity compensation plans not approved by security holders . .	—	—	—
Total . . . . .	206,000	\$1.09	504,742

- (1) At June 30, 2004 the number of shares of Common Stock available for incentive awards under the 2003 Stock Option Plan is 220,000 shares. The number of shares of Common Stock available for incentive awards under the 2003 Stock Incentive Plan is the greater of (a) 325,000 shares or (b) the number of share equal to five percent (5%) of the total number of shares of Common Stock from time to time outstanding.

## Purchases of Equity Securities

The Company purchased 25,000 shares from a director for \$40,260 in Fiscal 2004; 13,000 shares for \$21,060 (\$1.62 per share) in July 2003 and 12,000 shares for \$19,200 (\$1.60 per share) in October 2003.

## ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

### GENERAL

The Company's revenues are derived primarily from finance and service charges on secured, non-recourse loans ("pawn loans") and the proceeds from the sales of unredeemed merchandise

inventory ("merchandise sales"). The Company's pawn loans are generally made on the pledge of tangible personal property for one month, with automatic extension periods based on statutory requirements. All pawn loans are collateralized by tangible personal property placed in the possession of the Company, except for title loans. During the term of a title loan, the borrower is generally allowed to maintain possession of the collateral. See "Item 1. Description of Business—Continuing Store Operations—Lending." Pawn service charges are recognized when loans are repaid or renewed. If a loan is not repaid, the principal amount advanced on the loan, exclusive of any uncollected pawn service charges, becomes the carrying value of the forfeited collateral (inventory), which is recovered through sale.

## **CRITICAL ACCOUNTING POLICIES**

Management's Discussion and Analysis or Plan of Operation is based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, management evaluates its estimates and judgments, including those related to revenue recognition, inventories, allowance for losses on advances, long-lived and intangible assets, income taxes, contingencies and litigation. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions.

Management believes the following critical accounting policies affect its more significant judgments and estimates used in the preparation of its consolidated financial statements:

**FINANCE AND SERVICE CHARGE REVENUE RECOGNITION.** The Company accrues finance and service charge revenue on a constant-yield basis over the life of the loan on all pawn loans the Company deems collectible based on historical loan redemption statistics. If the pawn loan is not repaid, the principal amount becomes the carrying value of the forfeited collateral, which is recovered through sale. In the event the future performance of the loan portfolio differs significantly (positively or negatively) from expectations, revenue for the next reporting period would be likewise affected.

**INVENTORIES.** Inventories consist primarily of forfeited collateral from pawn loans not repaid. The carrying value of the forfeited collateral is stated at the lower of cost (cash amount loaned) or market. Because pawn loans are made without the borrower's personal liability, the Company does not investigate the creditworthiness of the borrower, but evaluates the pledged personal property as a basis for its lending decision. The amount the Company is willing to finance is typically based on a percentage of the pledged personal property's estimated disposition value. The sources for the Company's determination of the estimated disposition value are numerous and include the Company's internally published pricing guides, catalogues, "blue books," newspapers and previous disposition experience with similar items. The Company performs a physical count of its inventory at each location on a cyclical basis and reviews the composition of inventory by category and age in order to assess the carrying value of its inventories. Adverse changes in the disposition value of the Company's inventories may result in the need to write down its value.

**VALUATION OF LONG-LIVED AND INTANGIBLE ASSETS.** The Company assesses the impairment of long-lived and intangible assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors considered important which could trigger an impairment review include significant underperformance relative to expected historical

or projected future cash flows, significant changes in the manner of use of the acquired assets or the strategy for the overall business, and significant negative industry trends. When management determines that the carrying value of long-lived and intangible assets may not be recoverable, an impairment is measured based on the excess of the assets' carrying value over the estimated fair value.

**INCOME TAXES.** As part of the process of preparing the consolidated financial statements, the Company is required to estimate income taxes in each of the jurisdictions in which it operates. This process involves estimating the actual current tax exposure together with assessing temporary differences in recognition of income for tax and accounting purposes. These differences can result in deferred tax assets and liabilities. As of June 30, 2004 the Company has not recognized any deferred tax assets or liabilities. In accordance with American Institute of Certified Public Accountants Statement of Position 90-7, the Company recognized \$596,000 and \$197,000 of income tax expense and recorded a corresponding increase in additional paid in capital related to the utilization of net operating loss carryforwards previously unrecognized upon emergence from bankruptcy for the years ended June 30, 2004 and 2003, respectively.

**INVESTMENTS.** The Company accounts for its investment in American IronHorse on a cost basis. The investment of \$3,018,000 at June 30, 2004 is 9.7% of the equity of American IronHorse. Subsequent to June 30, 2004 the Company invested an additional \$1,395,000 in American IronHorse common stock \$600,000 of which is financed by the seller with a promissory note at 5% interest per annum requiring monthly payments of principal and interest of \$21,318 for 30 months beginning August 28, 2004. The additional investments increases its ownership to 13.9% of the equity of American IronHorse. The Company's other investments are accounted for as available for sale securities which results in the investments being carried at fair value on the balance sheet.

## **RESULTS OF OPERATIONS**

*For the Twelve Months Ended June 30, 2004 Compared to the Twelve Months Ended June 30, 2003*

Total revenues increased to \$20,534,000 from \$17,091,000 for the twelve months ended June 30, 2004 ("Fiscal 2004") compared to the twelve months ended June 30, 2003 ("Fiscal 2003"), a 20.1% increase. The increase is due primarily to increases in pawn service charges, increased merchandise sales and increased jewelry scrap sales. Merchandise sales for Fiscal 2004 were \$13,585,000 compared to \$11,481,000 for Fiscal 2003. The Company acquired one store and closed one store in Fiscal 2004. The new location contributed \$226,000 to the increase in total revenue.

In March 2004 the Company decided to close its store in South Carolina due to an unfavorable change in regulations effective January 2004 affecting automobile title loans. The impact on the Company's ability to recover defaulted collateral under the new regulations made the viability of operating one store in that market unfeasible. Store closing costs and impact on the Company's operations are insignificant. The store was closed in May 2004.

The Company earned management advisory and investment fees totaling \$344,000 during Fiscal 2004 related to the Company's investment in American IronHorse Motorcycle Company, Inc.

Gross profit in Fiscal 2004 increased to \$9,318,000 from \$8,921,000 for Fiscal 2003, a 4.5% increase. Gross profit as a percent of total revenue decreased to 45.4% in Fiscal 2004 compared to 52.2% for Fiscal 2003. The increase in gross profit is attributable to increased pawn service charges and increased sales volume due to aggressive discounting of merchandise sales prices. Gross profit on merchandise sales decreased \$942,000 or 28.5% to \$2,369,000 in Fiscal 2004, \$111,000 of which resulted from the new store.

Gross profit as a percent of merchandise sales will be affected by the Company's lending practices and ability to effectively implement its specialty retail strategies. Gross profit as a percent of

merchandise sales decreased 11.4% in Fiscal 2004 due to increased costs associated with the recovery and sale of cars on defaulted automobile title loans, write offs of defaulted automobile title loans, increased merchandise sales and higher related costs resulting from aggressively discounting sales prices.

Store operating expenses consist of all items directly related to the operation of stores, including salaries and related payroll costs, rent, property taxes, utilities, advertising, licenses, supplies, security costs, and other miscellaneous store expenses. Store operating expenses increased 9.8% to \$6,021,000, or 29.3% of total revenues, during Fiscal 2004 from \$5,484,000, or 32.1% of total revenues, during Fiscal 2003.

Corporate administrative expenses decreased 7.5% to \$3,074,000 during Fiscal 2004 from \$3,324,000 during Fiscal 2003 primarily due to reduced personnel expenses for bonuses earned in Fiscal 2003 and due to \$241,000 in reorganization expenses incurred related to the bankruptcy in Fiscal 2003. Corporate administrative expenses decreased to 15.0% of total revenues during Fiscal 2004 as compared to 19.4% during Fiscal 2003.

Interest expense increased \$422,000 from \$316,000 during Fiscal 2004 as compared to Fiscal 2003 primarily due to the reclassification of dividends as interest expense on redeemable preferred stock issued in conjunction in accordance with SFAS 150.

The Company also recognized a gain of \$2,046,000 on the sale of securities during Fiscal 2004 primarily due to the sale of its holdings in Sanders Morris Harris Group Inc. for \$4,998,000 in July 2003 which resulted in a \$1,630,000 gain.

The Company recognized income tax expense of \$614,000 during Fiscal 2004 compared to \$197,000 during Fiscal 2003. The income tax expense is principally related to the utilization of net operating loss carryforwards not previously recognized from bankruptcy.

The following table, as well as the discussion following, should be read in conjunction with "Item 7. Consolidated Financial Statements" and the notes thereto.

	<u>Fiscal 2004</u>	<u>Fiscal 2003</u>
Operating statement items as a percent of total revenues:		
Merchandise sales .....	66.1%	67.2%
Pawn service charges and related fee income .....	32.2	32.2
Management advisory and related fee income .....	1.7	0.6
Total revenues .....	100.0	100.0
Cost of sales .....	54.6	47.8
Store operating expenses .....	29.3	32.1
Corporate administrative expenses .....	15.0	19.4
Depreciation and amortization .....	2.3	1.9
Operating loss .....	(1.2)	(1.2)
Interest and dividend income .....	2.0	0.7
Interest expense .....	(3.5)	(1.9)
Gain on sale of investments .....	9.9	4.1
Income tax (provision) benefit .....	(3.0)	(1.2)
Net income (loss) .....	<u>4.2%</u>	<u>0.5%</u>

## LIQUIDITY AND CAPITAL RESOURCES

The Company's operations and growth have been financed with funds provided by the Merger in conjunction with the Plan, bank borrowings and funds generated from operations.

Under the terms of the Plan, the Company cancelled all equity interests as of the Confirmation Date, which included all common and preferred shareholder interests, and interests of any holders of options or warrants, and issued 2,079,948 shares of Common Stock to its unsecured creditors in exchange for cancellation of indebtedness upon completion of the Merger on August 30, 2002. The equity holders of CMHI received 1,071,636 shares of Series A Preferred Stock and 500,042 shares of Series B Preferred Stock. The Series B Preferred Stock is convertible at a ratio of approximately 3.44 shares of Common Stock for each share of Series B Preferred Stock to a total of 1,720,130 shares of Common Stock. As a result of the Merger, the Company received \$2,565,000 in cash and \$5,084,000 in marketable securities.

The Company obtained a new revolving credit facility from FCC, LLC, d/b/a First Capital, Kennesaw, Georgia (the "Lender"), in an amount up to \$4,500,000 (which replaced the Comerica line of credit), bears interest at the prevailing prime rate plus 2% (6% at June 30, 2004), and matures on June 17, 2007 (the "Credit Facility"). The Credit Facility is an asset-based loan with advances thereunder based on PawnMart's eligible accounts receivable and inventory, subject to a \$1,000,000 reserve and other reserves and adjustments. The Company was in compliance with the requirements and covenants as of June 30, 2004 and September 22, 2004. During Fiscal 2004 the Company paid fees associated with the Credit Facility totaling \$40,000.

As of June 30, 2004 the Company's primary sources of liquidity were \$206,000 in cash and cash equivalents, \$3,017,000 in marketable securities, \$73,000 in trade accounts receivable, \$489,000 in pawn service charges receivable, \$4,449,000 in pawn loan receivables, \$2,968,000 in inventories and \$78,000 in available and unused funds under the Credit Facility.

Net cash required by operations during Fiscal 2004 was \$1,052,000, which included \$10,000 in operating losses for its new store location.

The Company's profitability and liquidity is affected by the amount of loans outstanding, which is controlled in part by the Company's lending decisions. The Company is able to influence the frequency of forfeiture of collateral by increasing or decreasing the amount loaned in relation to the sales value of the pledged property. Tighter credit decisions generally result in smaller loans in relation to the estimated sales value of the pledged property and can thereby decrease the Company's aggregate loan balance and, consequently, decrease pawn service charges. Additionally, lower loans in relation to the pledged property's estimated sales value tend to slightly increase loan redemptions and improve the Company's liquidity. Conversely, providing higher loans in relation to the estimated sales value of the pledged property can result in an increase in the Company's pawn service charge income. Higher average loan balances can also result in a slight increase in loan forfeitures, which increases the quantity of goods on hand and, unless the Company increases inventory turnover, reduces the Company's liquidity.

The Company believes it has sufficient working capital to fund its current operations for Fiscal 2005.

The Series A Preferred Stock must be redeemed for cash at \$5.00 per share by the Company beginning April 30, 2005 in amounts of at least \$500,000 per year. Each April 30 thereafter through 2009 an additional 100,000 shares must be redeemed for cash at \$5.00 per share. On April 30, 2010 any unredeemed shares must be redeemed for cash at \$5.00 per share plus any accrued and unpaid dividends.

The following table summarizes the Company's contractual obligations at June 30, 2004, and the effect such obligations are expected to have on liquidity and cash flow in future periods, assuming the Credit Facility is not renewed or extended in future periods (in thousands):

	Credit Facility	Other Long Term Debt	Preferred Stock Redemption Requirement	Preferred Stock Dividend Requirement	Non- cancelable leases for continuing obligations	Total
2005 .....	—	121	500	389	1,228	2,238
2006 .....	—	118	500	364	1,009	1,991
2007 .....	2,785	120	500	339	848	4,592
2008 .....	—	24	500	314	802	1,640
2009 .....	—	—	500	289	473	1,262
Total .....	<u>\$2,785</u>	<u>\$383</u>	<u>\$2,500</u>	<u>\$1,695</u>	<u>\$4,360</u>	<u>\$11,723</u>

## RECENT ACCOUNTING PRONOUNCEMENTS

There are no recent accounting pronouncements expected to affect the Company.

## INFLATION

The Company does not believe inflation has had a material effect on its lending activities or its results of operations.

## SEASONALITY

The Company's retail operations are seasonal in nature with increased merchandise sales during the second and third fiscal quarters of each year. The Company's lending operations are also seasonal, with increased lending activities during the first and fourth fiscal quarters of each year.

## FACTORS THAT COULD AFFECT FUTURE PERFORMANCE

### *Availability of Qualified Store Management Personnel*

The Company's ability to expand may also be limited by the availability of qualified store management personnel. While the Company seeks to train existing qualified personnel for management positions and to create attractive compensation packages to retain existing management personnel, there can be no assurance that sufficient qualified personnel will be available to satisfy the Company's needs with respect to its planned expansion.

### *Competition*

The Company encounters significant competition in connection with the operation of its business. In connection with lending operations, the Company competes with other pawnshops (owned by individuals and by large operators) and certain financial institutions, such as consumer finance companies, which generally lend on an unsecured, as well as on a secured, basis. The Company's competitors in connection with its retail sales include numerous retail and discount stores. Many of the Company's competitors, including Cash America International, Inc., First Cash Financial Services, Inc., and EZCORP, Inc., have greater financial resources. These competitive conditions may adversely affect the Company's revenues, profitability and ability to expand.

### *Government Regulation*

The Company's lending operations are subject to extensive regulation, supervision and licensing under various federal, state and local statutes, ordinances and regulations. These statutes prescribe, among other things, service charges a pawnshop may charge for lending money and the rules of conduct that govern an entity's ability to maintain a pawnshop license. With respect to firearm and ammunition sales, a pawnshop must comply with the regulations promulgated by the United States Department of the Treasury, Bureau of Alcohol, Tobacco and Firearms. Governmental regulators have broad discretionary authority to refuse to grant a license or to suspend or revoke any or all existing licenses of licensees under common control if it is determined that any such licensee has violated any law or regulation or that the management of any such licensee is not suitable to operate pawnshops. The Company discontinued making loans on, buying or selling firearms in Fiscal 2003, but may have to comply with these regulations in the event stores are that are acquired have firearm inventory or pawn loans secured by firearms. In addition, there can be no assurance that additional state or federal statutes or regulations will not be enacted at some future date which could inhibit the Company's ability to expand, significantly decrease the service charges the Company can charge for lending money, or prohibit or more stringently regulate the sale of certain goods, such as firearms, any of which could significantly adversely affect the Company's prospects. In addition, the present statutory and regulatory environment of some states renders expansion into those states impractical. For instance, certain states require public sale of forfeited collateral or do not permit service charges sufficient to make pawnshop operations profitable.

### *Risks Related to Improper Assessment of the Pledged Property's Estimated Resale Value*

The Company makes pawn loans without the borrower's personal liability and does not investigate the creditworthiness of the borrower, but relies on the pledged personal property, and the possibility of its forfeiture, as a basis for its lending decision. In this regard, the recovery of the amount advanced, as well as realization of a profit on sale of merchandise, is dependent on the Company's initial assessment of the property's estimated resale value. Improper assessment of the resale value of the collateral can result in reduced marketability of the property and resale of the merchandise for an amount less than the amount advanced. Although, historically the Company has experienced profits from the sale of such merchandise, no assurances can be given that the Company's historical results will continue. For example, unexpected technological changes could adversely impact the value of consumer electronic products and declines in gold prices could reduce the resale value of jewelry items acquired in pawn transactions and could adversely affect the Company's ability to recover the amount advanced on the acquired collateral.

### *Dependence on Key Management*

The Company relies on the business and technical expertise of its executive officers and certain other key employees. The Company does not have an employment agreement with any member of its executive staff. The loss of the services of any of these individuals could have a material adverse effect on the Company's consolidated operating results. No assurance can be given that their services will be available in the future. The Company's success will also be dependent on its ability to attract and retain additional qualified management personnel.

### *Interest Rate Risk*

The Company is exposed to market risk in the form of interest rate risk. At June 30, 2004 the Company had \$2,785,000 outstanding under its Credit Facility with FCC, LLC. This Credit Facility is priced with a variable rate based on the prevailing prime rate plus 2%. See Note 7 of "Notes to Consolidated Financial Statements." Based on the average outstanding indebtedness during the year

ended June 30, 2004, a 10% increase in interest rates would have increased the Company's interest expense by approximately \$28,000 for Fiscal 2004.

The Company's cash and cash equivalents are invested in money market accounts and in other interest rate sensitive investments, including high yield bonds. Accordingly, the Company is subject to changes in market interest rates. However, the Company does not believe a change in these rates would have a material adverse effect on the Company's operating results, financial condition, and cash flows.

#### *Risks Related to Automobile Title Loans*

Georgia and South Carolina pawn regulations allow the Company to advance funds secured by automobile titles. Approximately 10.2% of the Company's total revenues during Fiscal 2004 were related to pawn service charges generated from such advances. During the term of the title loan, the borrower is allowed to maintain possession of the collateral unless the loan amount is in excess of \$5,000. In the event of default, the Company contracts to repossess the automobile and subsequently disposes of the automobile through its retail operations. Although the Company is exposed to the risk that it is unable to locate the collateral securing forfeited title loans, it has not historically experienced material adverse results from these instances and there can be no guarantee that material adverse results will not occur in the future. Further, the adoption of additional or the revision of existing laws and regulations impacting the Company's ability to advance funds secured by automobile titles could have a material adverse effect on the Company's business. The Company could also be subject to consumer claims and litigation seeking damages based upon wrongful repossession of automobiles.

#### *Issuance of Preferred Stock*

The Plan cancelled all outstanding equity interests in the Company for no value as of May 30, 2002. The Company's unsecured, non-priority creditors were issued 2,079,948 shares of Common Stock in the Company. As of June 30, 2004 there were 2,344,206 shares of Common Stock outstanding.

The Company's Amended and Restated Certificate of Incorporation authorizes the issuance of up to 2,500,000 shares of preferred stock with such rights and preferences as may be determined from time to time by the Board of Directors. Accordingly, the Board of Directors may, without stockholder approval, issue preferred stock with dividend, liquidation, conversion, voting, redemption or other rights which could adversely affect the voting power or other rights of the holders of the Company's Common Stock. The issuance of any shares of preferred stock having rights superior to those of the Company's Common Stock may result in a decrease in the value or market price of the Common Stock and could further be used by the Board as a device to prevent a change in control of the Company. Holders of the preferred stock may have the right to receive dividends, certain preferences and conversion rights.

Under the terms of the Plan, the Company merged with CMHI in exchange for two classes of Preferred Stock. The Series A Preferred Stock has a par value of \$0.01 per share and pays a \$0.25 per share cumulative cash dividend annually. The Company issued 1,071,636 shares of Series A Preferred Stock. The Series A Preferred Stock must be redeemed for cash at \$5.00 per share by the Company beginning April 30, 2005 in amounts of at least \$500,000 per year. Each April 30 thereafter through 2009 an additional 100,000 shares must be redeemed for cash at \$5.00 per share. On April 30, 2010 any unredeemed shares must be redeemed for cash at \$5.00 per share plus any accrued and unpaid dividends. The Company expects the Series A Preferred Stock to be classified as a liability in accordance with SFAS 150. See Note 9 of "Notes to Consolidated Financial Statements."

The CMHI shareholders also received 500,042 shares of Series B Preferred Stock that has a par value of \$0.01 and is convertible into 1,720,130 shares of Common Stock. The Series B Preferred Stock also pays a \$0.25 per share cumulative cash dividend annually.

## ITEM 7. CONSOLIDATED FINANCIAL STATEMENTS

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## **Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders  
Xponential, Inc.:

We have audited the accompanying consolidated balance sheet of Xponential, Inc. and subsidiaries as of June 30, 2004 and the related consolidated statements of operations, stockholders' equity (deficit), and cash flows year ended June 30, 2004, for the ten months ended June 30, 2003, and for the two months ended August 31, 2002. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Xponential, Inc. and subsidiaries as of June 30, 2004 and the results of their operations and their cash flows for the year ended June 30, 2004, the ten months ended June 30, 2003, and the two months ended August 31, 2002, in conformity with accounting principles generally accepted in the United States of America.

/s/ GRANT THORNTON, LLP

Dallas, Texas  
September 1, 2004

# XPONENTIAL, INC. AND SUBSIDIARIES

## Consolidated Balance Sheet

June 30, 2004

(In Thousands)

### Assets

#### Current assets:

Cash and cash equivalents	\$ 206
Accounts receivable	73
Pawn service charges receivable	489
Pawn loans receivable	4,449
Inventories	2,968
Investments	3,017
Prepaid expenses and other current assets	275

Total current assets 11,477

Property and equipment	869
Intangible assets	35
Investment in American IronHorse Motorcycle Company, Inc.	3,018
Other assets	155

Total assets \$15,554

### Liabilities and Stockholders' Equity

#### Current liabilities:

Current maturities of notes payable	\$ 121
Accounts payable	65
Accrued payroll and payroll taxes	265
Deferred revenue	93
Other accrued expenses	273

Total current liabilities 817

Long term notes payable	3,050
	<u>3,867</u>

Commitments and contingencies —

#### Redeemable preferred stock:

Preferred stock—Series A; \$0.01 par value, 1,250,000 shares authorized; 5% cumulative dividend, liquidation preference \$5.00 per share; 1,071,636 shares issued and outstanding	5,358
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#### Stockholders' equity

Preferred stock—Series B; convertible, 500,050 shares authorized; 5% cumulative dividend, liquidation preference \$5.00 per share; 500,042 shares issued and outstanding	5
Common stock \$0.01 par value; 10,000,000 shares authorized; 2,344,206 issued	24
Treasury Stock	(40)
Additional paid-in capital	5,319
Retained earnings	740
Accumulated other comprehensive income	281

Total stockholders' equity 6,329

Total liabilities and stockholders' equity \$15,554

See accompanying notes to consolidated financial statements.

**XPONENTIAL, INC. AND SUBSIDIARIES**

**Consolidated Statements of Operations**

**(In Thousands, Except Per Share Data)**

	<u>Reorganized Company</u>	<u>Reorganized Company</u>	<u>Predecessor</u>
	<u>For the Year Ended June 30, 2004</u>	<u>For the Ten Months Ended June 30, 2003</u>	<u>For the Two Months Ended August 31, 2002</u>
Revenues:			
Merchandise sales .....	\$13,585	\$ 9,903	\$ 1,578
Pawn service charges and related fee income .....	6,605	4,643	853
Management advisory and related fee income .....	344	76	38
Total revenues .....	20,534	14,622	2,469
Expenses:			
Cost of sales .....	11,216	7,095	1,075
Store operating expenses .....	6,021	4,588	896
Corporate administrative expenses .....	3,074	2,747	336
Depreciation and amortization .....	473	265	63
Total expenses .....	20,784	14,695	2,370
Operating income (loss) .....	(250)	(73)	99
Interest and dividend income .....	423	123	—
Interest expense .....	(738)	(233)	(83)
Gain on disposition of assets .....	5	2	—
Gain on sale of investments .....	2,046	699	—
Reorganization expenses .....	—	—	(241)
Income (loss) from continuing operations .....	1,486	518	(225)
Extraordinary items:			
Gain on debt discharge .....	—	—	11,810
Net income before income taxes .....	1,486	518	11,585
Income tax provision .....	614	197	—
Net income .....	872	321	11,585
Preferred stock dividend requirement .....	(125)	(328)	—
Net income (loss) allocable to common stockholders	<u>\$ 747</u>	<u>\$ (7)</u>	<u>\$11,585</u>
Income (loss) per common share:			
Basic			
Continuing operations .....	\$ 0.32	\$ —	\$ (0.09)
Extraordinary items .....	—	—	4.72
	<u>\$ 0.32</u>	<u>\$ —</u>	<u>\$ 4.63</u>
Diluted			
Continuing operations .....	\$ 0.21	\$ —	\$ (0.09)
Extraordinary items .....	—	—	4.72
	<u>\$ 0.21</u>	<u>\$ —</u>	<u>\$ 4.63</u>

See accompanying notes to consolidated financial statements.

**XPONENTIAL, INC. AND SUBSIDIARIES**

**Consolidated Statements of Stockholders' Equity (Deficit)**  
**Years Ended June 30, 2004, June 30, 2003 and June 30, 2002**  
**(In Thousands, Except Share Data)**

	Preferred stock		Common stock		Series A redeemable common stock purchase warrants		Series B redeemable common stock purchase warrants		Additional common stock purchase warrants		Additional paid-in capital		Retained Earnings (Accumulated deficit)		Other Comprehensive Income		Treasury stock		Total stockholders' equity (deficit)	
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount										
Balance at July 1, 2002	416,667	2,500	2,503,149	25	1,974,060	249	1,380,000	86	60	22,004		(33,407)		(70)				(8,553)		
Net Income	—	—	—	—	—	—	—	—	—	—		11,585		—				11,585		
Debt Discharge and Fresh Start Adjustments	(416,667)	(2,500)	(423,201)	(4)	(1,974,060)	(249)	(1,380,000)	(86)	(60)	(20,152)		21,822		70				(1,159)		
Issuance of Preferred Stock in Connection with Merger	500,042	5	—	—	—	—	—	—	—	2,345		—		—				2,350		
Balance at August 31, 2002	500,042	5	2,079,948	21	—	—	—	—	—	4,197		—		—				4,223		
Amortization of Stock Options Issued Tax Expenses Allocated to Additional Paid in Capital Related to Bankruptcy	—	—	—	—	—	—	—	—	—	197		—		—				197		
Preferred Stock Dividends paid	—	—	—	—	—	—	—	—	—	—		(328)		—				(328)		
Net Income	—	—	—	—	—	—	—	—	—	—		321		—				321		
Other Comprehensive Income	—	—	—	—	—	—	—	—	—	—		—		—				—		
Unrealized Gain on Investments	—	—	—	—	—	—	—	—	—	—		—		—				1,758		
Comprehensive Income	—	—	—	—	—	—	—	—	—	—		(7)		—				—		
Balance at June 30, 2003	500,042	5	2,079,948	21	—	—	—	—	—	4,403		(7)		—				6,180		
Amortization of Stock Options Issued Tax Expenses Allocated to Additional Paid in Capital Related to Bankruptcy	—	—	—	—	—	—	—	—	—	5		—		—				5		
Purchase of Common Stock	—	—	285,258	3	—	—	—	—	—	596		—		—				596		
Purchase of Treasury Stock	—	—	(25,000)	—	—	—	—	—	—	315		—		—				318		
Preferred stock dividends paid	—	—	—	—	—	—	—	—	—	—		(125)		(40)				(40)		
Net Income	—	—	—	—	—	—	—	—	—	—		872		—				(125)		
Other Comprehensive Income	—	—	—	—	—	—	—	—	—	—		—		—				872		
Reclassification of unrealized gains recognized in net income	—	—	—	—	—	—	—	—	—	—		—		—				—		
Unrealized Gain on Investments	—	—	—	—	—	—	—	—	—	—		—		—				(2,046)		
Comprehensive Income	—	—	—	—	—	—	—	—	—	—		747		—				569		
Balance at June 30, 2004	500,042	5	2,344,206	24	—	—	—	—	—	5,319		740		—				(1,477)		
														—				(730)		
														—				6,329		
														(40)				(40)		

See accompanying notes to consolidated financial statements.

**XPONENTIAL, INC. AND SUBSIDIARIES**

**Consolidated Statements of Cash Flows**

**(In Thousands)**

	<u>Reorganized Company</u>	<u>Reorganized Company</u>	<u>Predecessor</u>
	<u>For the Year Ended June 30, 2004</u>	<u>For the Ten Months Ended June 30, 2003</u>	<u>For the Two Months Ended August 31, 2002</u>
Cash flows from operating activities:			
Net income .....	\$ 872	\$ 321	\$ 11,585
Adjustments to reconcile net income to net cash used in operating activities:			
Depreciation and amortization .....	473	265	63
Non-cash compensation expense .....	5	9	—
Gain on debt discharge .....	—	—	(11,810)
Gain on sale of investments .....	(2,046)	—	—
Deferred income tax expense .....	596	197	—
Changes in operating assets and liabilities, net of effect of acquisition and merger:			
Accounts receivable .....	103	(79)	(24)
Pawn service charges receivable .....	14	(128)	(45)
Inventories, net .....	(428)	73	62
Prepaid expenses and other current assets .....	(317)	(68)	(3)
Prepetition liabilities, accounts payable and accrued liabilities .....	(321)	219	(56)
Net cash provided by (used in) operating activities .....	<u>(1,049)</u>	<u>809</u>	<u>(228)</u>
Cash flows from investing activities:			
Pawn loans made, net .....	122	(1,156)	(414)
Acquisition of stores .....	(32)	(112)	—
Proceeds from Sale of investments .....	8,711	2,780	—
Purchases of investments .....	(6,214)	(3,641)	—
Purchases of property and equipment .....	(407)	(432)	—
Net cash provided by (used in) investing activities .....	<u>2,180</u>	<u>(2,561)</u>	<u>(414)</u>
Cash flows from financing activities:			
Cash acquired in merger .....	—	2,565	—
Principal payments on notes payable .....	(15,581)	—	—
Borrowings on notes payable .....	14,283	(455)	455
Proceeds from sale of common stock .....	318	—	—
Purchase of treasury stock .....	(40)	—	—
Dividends paid .....	(125)	(328)	—
Net cash provided by (used in) financing activities .....	<u>(1,145)</u>	<u>1,782</u>	<u>455</u>
Net increase (decrease) in cash and cash equivalents .	(14)	30	(187)
Cash and cash equivalents at beginning of period . . .	220	190	377
Cash and cash equivalents at end of period .....	<u>\$ 206</u>	<u>\$ 220</u>	<u>\$ 190</u>
Supplemental disclosures of cash flow information—			
Cash paid for interest .....	<u>\$ 608</u>	<u>\$ 218</u>	<u>\$ 83</u>

See accompanying notes to consolidated financial statements.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements**  
**June 30, 2004**

**(1) Organization and Business**

Xponential, Inc., formerly PawnMart, Inc. (the "Company"), was incorporated in Delaware on January 13, 1994. Effective February 28, 2003, the Company changed its name to "Xponential, Inc." The Company's wholly owned subsidiary PawnMart, Inc. is a specialty finance and retail enterprise principally engaged in establishing and operating stores which advance money secured by the pledge of tangible personal property, and buying and selling pre-owned merchandise. As of June 30, 2004, the Company owned and operated 26 stores located in Georgia and North Carolina.

On July 9, 2001 (the "Petition Date"), the Company filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Northern District of Texas, Fort Worth Division (the "Bankruptcy Court") in the case of PawnMart, Inc., Debtor, Case No. 01-44957-BJH-11. On May 20, 2002 (the "Confirmation Date"), the Bankruptcy Court entered an order (the "Confirmation Order") confirming the Company's first amended plan of reorganization (the "Plan"). The Plan became effective on May 31, 2002 (the "Effective Date").

The Company successfully emerged from bankruptcy on August 30, 2002 when it consummated a merger (the "Merger") with C/M Holdings, Inc. ("CMHI"). The reorganized Company adopted fresh-start reporting and gave effect to its emergence from bankruptcy and consummation of the Plan on August 30, 2002. There was no reorganization value in excess of amounts allocated to identifiable assets.

**(2) Summary of Significant Accounting Policies**

**(a) Basis of Presentation and Fiscal Years**

The consolidated financial statements include the financial statements of the Company and its wholly owned subsidiary, PawnMart, Inc. All significant intercompany balances and transactions have been eliminated in consolidation.

Management of the Company makes estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (US GAAP). Actual results could differ from those estimates.

The Board of Directors of the Company determined in May 2002 that it was in the Company's best interest to change its fiscal year end from the Saturday nearest January 31 to June 30 to more accurately reflect the Company's post bankruptcy operating results. The change in fiscal year end was effective June 30, 2002.

**(b) Fresh-start Reporting**

The accompanying financial statements have been prepared in accordance with US GAAP includes the American Institute of Certified Public Accountants Statement of Position 90-7: "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code" ("SOP 90-7").

Fresh-start reporting as set forth in SOP 90-7 requires that the reorganized Company restate its assets and liabilities to reflect their reorganization value, which approximates fair value at the date of the reorganization. In so restating, SOP 90-7 required the reorganized Company to allocate its

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(2) Summary of Significant Accounting Policies (Continued)**

reorganization value to its assets based upon their estimated fair value. Each liability existing on the Confirmation Date was to be stated at the present value of amounts to be paid, determined using an appropriate discount rate.

**(c) Cash and Cash Equivalents**

The Company considers any highly liquid investments with original maturities of three months or less to be cash equivalents.

**(d) Loans and Revenue Recognition**

Pawn loans (loans) are generally made on the pledge of tangible personal property for one month, with an automatic extension period from ten to sixty days in accordance with statutory requirements except for loans on auto titles which have shorter extension periods. Pawn service charges are accrued on a constant-yield basis over the life of the loan on all pawn loans the Company deems collectible based on historical loan redemption statistics. If a loan is not repaid, the principal amount advanced on the loan, or the fair value of the collateral, if lower, exclusive of any uncollected pawn service charges, becomes the carrying value of the forfeited collateral (inventories), which is recovered through sale.

Pawn service charges receivable represent an amount equivalent to one month's earned pawn service charges, net of an allowance for pawn service charges deemed uncollectible, based on the Company's historical loan redemption rate.

Merchandise sales consist of direct sales of merchandise to customers. Sales are recognized when title and risk of loss have passed to the customer, which is generally at the point of sale.

**(e) Investments**

Investments consist of marketable debt and equity securities available for sale. Available for sale securities are measured at fair value, with net unrealized gains and losses reported in accumulated other comprehensive as a component of stockholders' equity.

**(f) Inventories**

Inventories are recorded at cost and represent merchandise acquired from forfeited loans, merchandise purchased directly from the public and merchandise purchased from vendors. The cost of inventories is determined on the specific identification method. Inventories are stated at the lower of cost or market. Interim payments from customers on layaway sales are credited to deferred revenue and subsequently recorded as income during the period in which final payment is received. Deferred revenues related to layaway sales totaled approximately \$93,000 and \$83,000 as of June 30, 2004 and 2003, respectively and are included in other accrued expenses in the accompanying consolidated balance sheets.

**(g) Property and Equipment**

Property and equipment are recorded at cost. Depreciation is determined on the straight-line method based on estimated useful lives of two to seven years for equipment. The costs of improvements on leased stores are capitalized as leasehold improvements and are amortized on the straight-line method over the shorter of the lease term or their estimated useful lives. The cost of

**XPONENTIAL, INC.**

**Notes To Consolidated Financial Statements (Continued)**

**June 30, 2004**

**(2) Summary of Significant Accounting Policies (Continued)**

property retired or sold and the related accumulated depreciation is removed from the accounts and any resulting gain or loss is recorded in the results of operations in the period retired.

The Company determines whether its property and equipment is impaired whenever events or circumstances indicate the carrying amount of its property and equipment may not be recoverable. Recoverability is measured by a comparison of the carrying amount to future undiscounted net cash flows expected to be generated. If the carrying amount exceeds its estimated future net cash flows, an impairment charge is recognized by the amount by which the carrying amount of the assets exceeds the fair value of the asset.

**(h) Intangible Assets**

Intangible assets consist of customer lists and are amortized over a two year period using the straight-line method. Intangible assets amounted to \$36,000, net of \$42,000 of accumulated amortization as of June 30, 2004 and are included in other assets.

**(i) Investment in American IronHorse Motorcycle Company, Inc.**

The Company has invested in \$3,018,000 in American IronHorse Motorcycle Company, Inc. ("American IronHorse") as June 30, 2004. The Company owns 9.7% of the equity of American IronHorse and accounts for this investment as a non current asset on the cost basis. The Company invested an additional \$1,395,000 in American IronHorse common stock, subsequent to June 30, 2004 increasing its ownership to 13.9% of American IronHorse's equity. \$600,000 of the investment is financed by the seller with a promissory note at 5% interest per annum requiring monthly payments of principal and interest of \$21,318 for 30 months beginning August 28, 2004. It is possible that the Company may increase its investment in American IronHorse and the accounting for the investment may change as a result of increased investments.

**(j) Income Taxes**

The Company and its subsidiary file a consolidated Federal income tax return. Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the fiscal years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation account is used to reduce the net deferred tax assets to amounts expected to be realized. In accordance with SOP 90-7, the Company records income tax expense with a credit to additional paid in capital when net operating loss carryforwards not previously recognized upon the emergence from bankruptcy are used to offset taxable income generated by the successor company.

**(k) Advertising Costs**

Advertising costs are expensed the first time advertising takes place. Advertising expense was approximately \$32,000 and \$30,000 for the fiscal years ended June 30, 2004 and 2003, respectively.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(2) Summary of Significant Accounting Policies (Continued)**

**(l) Fair Values of Financial Instruments**

Pawn loans are outstanding for a relatively short period of time, generally 90 days or less, depending on local regulations. The rate of finance and service charge is determined by regulatory guidelines and bears no valuation relationship to interest rate market movements. For these reasons, management believes that the fair value of pawn loans approximates their carrying value. The Company's revolving line of credit with Comerica Bank bears interest at a variable rate that is frequently adjusted on the basis of market rate changes and is equal to rates available for debt with similar characteristics. Accordingly, management believes that the carrying value of such debt approximates its fair value. The fair values of the Company's remaining long-term notes payable instruments could not be determined due to the financial condition of the Company and the likelihood of repayment of such debt. The carrying amount of all other financial instruments including cash, receivables and payables included in the Company's consolidated balance sheet approximate fair value due to the short maturity of these instruments.

**(m) Stock Based Compensation**

Effective January 1, 2003, the Company adopted the fair value method defined in SFAS No. 123, "Accounting for Stock-Based Compensation," in accounting for its stock option plans, where previously the Predecessor Company applied Accounting Principles Board's Opinion No. 25, ("APB No. 25"), "Accounting for Stock Issued to Employees," and related Interpretations. SFAS No. 123 indicates that the fair value method is the preferable method of accounting, and the Company has elected to apply it for all options granted for the reorganized company after August 31, 2002. Under APB No. 25, compensation costs related to stock options issued pursuant to compensatory plans are measured based on the difference between the quoted market price of the stock at the measurement date (ordinarily the date of grant) and the exercise price and should be charged to expense over the periods during which the grantee performs the related services. No stock-based employee compensation expense was recognized in the period ended February 2, 2002. All outstanding stock option grants of the Predecessor Company were cancelled in accordance with the Company's reorganization plan which was confirmed on May 20, 2002.

**(n) Net Income (Loss) Per Common Share**

Basic net income (loss) per common share is based upon the weighted average number of common shares outstanding during each period presented. Diluted income for common shares are based upon the weighted average number of common shares outstanding during the period, plus, if dilutive, the assumed exercise of stock options and the conversion of convertible securities during the beginning of the year, or for the period outstanding during the year.

**(o) Segment Information**

Statement of Financial Accounting Standards No. 131, "Disclosures About Segments of an Enterprise and Related Information" (Statement No. 131) establishes standards for the way public business enterprises are to report information about operating segments. The Company defines each of its stores as operating segments; however, management has determined that all of its stores have similar economic characteristics and also meet the other criteria which permit the stores to be aggregated into one reportable segment.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(3) Recent Accounting Pronouncements**

In January 2003, the FASB issued FIN 46, "Consolidation of Variable Interest Entities." FIN 46 clarifies the application of Accounting Research Bulletin 51, "Consolidated Financial Statements," for certain entities that do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties or in which equity investors do not have the characteristics of a controlling financial interest ("variable interest entities"). Variable interest entities within the scope of FIN 46 will be required to be consolidated by their primary beneficiary. The primary beneficiary of a variable interest entity is determined to be the party that absorbs a majority of the entity's expected losses, receives a majority of its expected returns, or both. FIN 46 applies immediately to variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. It applies in the first fiscal year or interim period beginning after June 15, 2003, to variable interest entities in which an enterprise holds a variable interest that it acquired before February 1, 2003. The adoption of the provisions of FIN 46 did not have a material impact upon the Company's financial condition or results of operations.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity", ("SFAS 150"). This statement establishes standards for how an issuer classifies and measures in its statement of financial position certain financial instruments with characteristics of both liabilities and equity. In accordance with the standard, financial instruments that embody obligations for the issuer are required to be classified as liabilities. This Statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. Our Series A Preferred Stock was reclassified as a liability as of July 1, 2003 and dividends are classified as interest expense.

**(4) Bankruptcy**

As described in Note (1) the Company filed for bankruptcy on July 9, 2001. In the Chapter 11 proceedings, substantially all liabilities as of the Petition Date were subject to compromise under the Plan.

Under the terms of the Plan, the Company cancelled all equity interests of its common and preferred shareholders and interests of any holders of options and warrants. The Company issued 2,079,948 shares of Common Stock to its unsecured creditors in exchange for cancellation of indebtedness. The Company issued In connection with the Merger with CMHI, the Company issued 1,071,636 shares of Series A Preferred Stock and 500,042 Series B Preferred Stock to the former shareholders of CMHI, which was owned in part by Dwayne A. Moyers and Jeffrey A. Cummer, officers and directors of the Company and by Carroll Dawson, a director of the Company. At the time of the Merger, CMHI did not have any business operations and principally held investments.

The Bankruptcy Court confirmed the Plan on May 20, 2002 with an Effective Date of May 31, 2002. The consummation of the Plan was contingent on several material events including consummation of the Merger which occurred on August 30, 2002 which is reported herein as a material business combination. The Company acquired 100 percent of the outstanding common stock of CMHI on August 30, 2002. The results of CMHI's operations have been included in the financial statements since the date of the Merger.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(4) Bankruptcy (Continued)**

The Company adopted fresh-start reporting because holders of existing voting shares immediately before confirmation of the Plan received less than 50% of the voting shares of the emerging entity; (all pre-confirmation equity interests were cancelled), and the reorganization value is less than the postpetition liabilities and allowed claims, as shown below.

The reorganization value of approximately \$7.6 million resulted in a net value of approximately \$1.9 million to the new common equity holders after allowance for post confirmation liabilities of the reorganized Company of \$5.7 million. The reorganization value was determined in consideration of several factors and by reliance on various valuation methods including discounted cash flow, book value multiples of comparable companies in its industry, net realizable value of asset sales and other applicable methods. The calculated reorganization value was based on estimates and assumptions about circumstances in a relatively high-risk investment scenario that have not yet taken place in which there are significant economic and competitive uncertainties beyond the control of the reorganized Company. The Company assigned no value to the Company's net operating loss carryovers in the calculation of its reorganization value due to the lack of certainty of utilizing the net operating loss based on historical operating results and the potential limitations on use resulting from the Plan.

	(in thousands)
Postpetition current liabilities .....	\$ 5,145
Liabilities deferred pursuant to the Plan .....	700
Liabilities exchanged for equity in the reorganized Company .....	11,810
Total postpetition liabilities and allowed claims .....	17,655
Reorganization value .....	7,567
Excess of liabilities over reorganization value .....	<u>\$10,088</u>

After consideration of the Company's debt capacity, extensive negotiations among parties in interest, projected earnings before interest and taxes, free cash flow to interest and debt service and other capital considerations, it was agreed the Company's organization capital structure prior to the Merger, is as follows:

	At August 30, 2002 (in thousands)
Postpetition current liabilities .....	\$1,274
Notes payable—priority tax claims(1) .....	700
Post confirmation bank line of credit .....	3,720
Common stock .....	1,873
	<u>\$7,567</u>

- (1) Approximately \$95,000 due in cash and \$605,000 payable in quarter installments of approximately \$100,000 per year at 7% interest per annum.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(4) Bankruptcy (Continued)**

The effects of the Plan on the Company's balance sheet as of August 30, 2002 is as follows:

(in thousands)	Prior to Plan Consummation	Debt Discharge	Fresh Start Adjustments	Reorganized Balance Sheet Prior to Merger
<i>Assets</i>				
Current Assets				
Cash and cash equivalents . . . . .	\$ 190	\$ —	\$ —	\$ 190
Receivables . . . . .	61	—	—	61
Pawn loan receivables . . . . .	3,790	—	—	3,790
Inventory—net . . . . .	2,554	—	—	2,554
Prepaid expenses and other current assets . . . . .	177	—	—	177
Total current assets . . . . .	6,772	—	—	6,772
Property and equipment, net . . . . .	834	—	(160)	674
Debt issuance costs, net . . . . .	1,000	—	(1,000)	—
Other assets, net . . . . .	121	—	—	121
Total assets . . . . .	<u>\$ 8,727</u>	<u>\$ —</u>	<u>\$ (1,160)</u>	<u>\$7,567</u>
<i>Liabilities and Stockholders' Equity (Deficit)</i>				
Current liabilities				
Accounts payable and accrued liabilities . . . . .	\$ 674	\$ —	\$ —	\$ 674
Notes payable—prepetition taxes, current portion . . . . .	—	195	—	195
Prepetition liabilities . . . . .	12,510	(12,510)	—	—
Notes payable—bank line of credit . . . . .	3,720	(3,720)	—	—
Notes payable . . . . .	600	—	—	600
Total current liabilities . . . . .	17,504	(16,035)	—	1,469
Long term debt				
Notes payable—prepetition taxes, net of current portion . . . . .	—	505	—	505
Notes payable—bank line of credit . . . . .	—	3,720	—	3,720
Total liabilities . . . . .	17,504	(11,810)	—	5,694
Stockholders' equity (deficit)				
Preferred stock (old) . . . . .	2,500	(2,500)	—	—
Common stock (new) . . . . .	—	21	—	21
Common stock (old) . . . . .	25	(25)	—	—
Series A redeemable Common Stock purchase warrants . . . . .	249	(249)	—	—
Series B redeemable Common Stock purchase warrants . . . . .	86	(86)	—	—
Additional Common Stock purchase warrants . . . . .	60	(60)	—	—
Additional paid-in capital . . . . .	22,004	2,829	(22,981)	1,852
Accumulated deficit . . . . .	(33,631)	11,810	21,821	—
Less treasury stock, at cost (old) . . . . .	(70)	70	—	—
Total stockholders' equity (deficit) . . . . .	<u>(8,777)</u>	<u>11,810</u>	<u>(1,160)</u>	<u>1,873</u>
Total liabilities and stockholders' equity (deficit) . . . . .	<u>\$ 8,727</u>	<u>\$ —</u>	<u>\$ (1,160)</u>	<u>\$7,567</u>

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(4) Bankruptcy (Continued)**

On August 30, 2002, the Company acquired 100 percent of the outstanding common shares of C/M Holdings, Inc. ("CMHI") pursuant to the Plan.

The aggregate purchase price for CMHI was approximately \$7.8 million which was paid through the issuance of Series A and Series B Preferred Stock valued at \$5.3 million and \$2.5 million, respectively. The value of the Preferred Stock was based on liquidation preferences and dividend and conversion features.

The following table summarizes the estimated value of the acquired assets and liabilities assumed at the date of the Merger.

	<u>At August 30, 2002</u> (in thousands)
Current assets .....	\$2,725
Property and equipment, net .....	36
Investments, primarily common stock .....	5,117
Total assets acquired .....	7,878
Total liabilities assumed .....	20
Net assets acquired .....	<u>\$7,858</u>

The following is a condensed consolidated balance sheet August 30, 2002 (unaudited), which reflects the Merger:

<u>(in thousands)</u>	<u>Xponential, Inc.</u> <u>Reorganized</u> <u>Balance Sheet</u> <u>Prior to Merger</u>	<u>CMHI Assets</u> <u>Acquired and</u> <u>Liabilities</u> <u>Assumed as</u> <u>of 8/30/2002</u>	<u>Reorganized</u> <u>Balance Sheet</u> <u>After Merger</u>
<i>Assets</i>			
Current assets .....	\$6,772	\$2,725	\$ 9,497
Property and equipment, net .....	674	36	710
Other assets .....	121	5,117	5,238
Total assets .....	<u>\$7,567</u>	<u>\$7,878</u>	<u>\$15,445</u>
<i>Liabilities and stockholders' equity</i>			
Current liabilities .....	\$1,469	\$ 170(1)	\$ 1,639
Notes payable .....	4,225	—	4,225
	5,694	170	5,864
Redeemable preferred stock .....	—	5,358	5,358
Stockholders' equity:			
Preferred stock .....	—	5	5
Common stock .....	21	—	21
Additional paid in capital .....	1,852	2,345	4,197
Total liabilities and stockholders' equity .....	<u>\$7,567</u>	<u>\$7,878</u>	<u>\$15,445</u>

(1) Includes \$150,000 investment banking fee to related parties payable on completion of Merger.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(5) Asset Acquisitions**

During the fiscal year ended June 30, 2004, the Company acquired the assets of one pawnshop in purchase transactions for an aggregate cash purchase price of \$142,000. The purchase price for the acquisitions was determined based upon the historical volume of annual loan and sales transactions, inventory on hand, condition of property and equipment, quality and condition of the location, and projected future operating results.

All purchase transactions have been accounted for using the purchase method of accounting. Accordingly, the purchase price was allocated to assets and liabilities acquired based upon their estimated fair market values at the dates of acquisition. The purchase price was allocated to the tangible assets and intangible assets based on their fair market value as follows:

Pawn loan receivables . . . . .	\$ 42
Property and equipment, net . . . . .	68
Customer list . . . . .	<u>32</u>
Net assets acquired . . . . .	<u>\$142</u>

The results of operations of the acquisitions have been included in the consolidated financial statements from their respective dates of acquisition.

**(6) Property and Equipment**

Property and equipment consists of the following at June 30, 2004, (in thousands):

	Years of Useful life	June 30, 2004
Automobiles . . . . .	5	\$ 175
Furniture and equipment . . . . .	5-7	782
Leasehold improvements . . . . .	3-10	<u>517</u>
		1,474
Less: accumulated depreciation and amortization . . . . .		<u>(605)</u>
		<u>\$ 869</u>

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(7) Notes Payable**

Notes payable consist of the following at June 30, 2004 (in thousands):

Revolving line of credit with a bank, bearing interest at prime plus two percent (6% at June 30, 2004) payable monthly, to mature June 17, 2007, collateralized by substantially all of the assets of PawnMart, Inc., the Company's wholly owned subsidiary and guaranteed by the Company . . . .	\$2,785
Notes payable with a vendor, bearing interest at 7%, collateralized by computer software, payable monthly, to mature on September 30, 2004 . .	12
Other unsecured notes payable . . . . .	374
	<u>3,171</u>
Less: current maturities . . . . .	<u>(121)</u>
Long term notes payable . . . . .	<u>\$3,050</u>

The Company obtained a new revolving credit facility on June 17, 2004 from FCC, LLC, d/b/a First Capital, Kennesaw, Georgia (the "Lender"), in an amount up to \$4,500,000 (which replaced the Comerica line of credit), bears interest at the prevailing prime rate plus 2.00% (6% at June 30, 2004), and matures on June 17, 2007 (the "Credit Facility"). The Credit Facility is an asset-based loan with advances thereunder based on PawnMart's eligible accounts receivable and inventory, subject to a \$1,000,000 reserve and other reserves and adjustments. The Credit Facility is collateralized by substantially all of the unencumbered assets of PawnMart, Inc., the Company's subsidiary and is guaranteed by the Company. The Company is required to maintain certain financial ratios and is prohibited from paying cash dividends on its common stock unless specifically approved by the Lender.

The Company paid off its \$4,000,000 credit facility with Comerica Bank (the "Bank") that was to mature on June 30, 2004 and which accrued interest at 9% per annum (the "Credit Facility"), subject to monthly mandatory principal reductions each in the amount of \$100,000 commencing February 1, 2004 through and including June 1, 2004. Amounts available under the Credit Facility were limited to certain percentages of pawn loans, inventories, and pawn service charges receivable. The Credit Facility was collateralized by substantially all of the unencumbered assets of the Company and PawnMart. The Company also pledged additional collateral in the form of marketable and other securities to the Bank in the amount of \$2,500,000.

The Company financed \$65,000 of its new computer system software with a vendor over a two year period beginning September 2002. The note bears interest at a rate of seven percent per annum. The remaining amount due of \$12,000 as of June 30, 2004 is classified as a current liability.

The Company also compromised certain priority tax claims in the amount of \$621,000 in its reorganization plan agreeing to amortize the claims over a six year period from the date of assessment in quarterly installments of approximately \$35,000 including interest at the rate of seven percent per annum. The current and long term portions due as of June 30, 2004 were \$109,000 and \$265,000, respectively.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(8) Income Taxes**

The tax effects of temporary differences and carryforwards that give rise to significant portions of the deferred tax assets and deferred tax liabilities at June 30, 2004 are presented below (in thousands):

	<u>June 30, 2004</u>
Deferred tax assets:	
Net operating loss carryforwards . . . . .	\$ 4,249
Property and equipment . . . . .	173
Inventories . . . . .	114
Goodwill and other intangible assets . . . . .	27
Total gross deferred tax assets . . . . .	4,563
Less valuation allowance . . . . .	(4,563)
Net deferred tax assets . . . . .	<u>—</u>

The provisions for income taxes differs from amounts determined by applying the expected federal statutory tax rate to income from continuing operations before income taxes. Following is a reconciliation of such differences (in thousands):

	<u>For the Year Ended June 30, 2004</u>	<u>For the Ten Months Ended June 30, 2003</u>	<u>For the Two Months Ended August 30, 2002</u>
Tax at federal statutory rates . . . . .	\$ 541	\$ 176	\$ 3,944
State and local income taxes (benefit), net of federal tax benefit . . . . .	73	21	(14)
	614	197	3,930
Change in valuation allowance . . . . .	(596)	(197)	(3,930)
Tax expense allocated to Additional Paid in Capital related to bankruptcy . . . . .	596	197	—
	<u>\$ 614</u>	<u>\$ 197</u>	<u>\$ —</u>

At June 30, 2004 the Company has net operating loss carryforwards for tax purposes of approximately \$12,498,000 including approximately \$2,039,000 of capital loss carryforward which may be used only to offset future capital gains. During Fiscal 2003, the Company recognized income of approximately \$11,800,000 due to discharge of indebtedness in conjunction with the confirmation of the Company's bankruptcy plan. A formal legal or tax opinion on the effects of the Company's bankruptcy proceedings on the survival of the net operating loss carryforwards, their future availability, or any limitation on the utilization of these net operating loss carryforwards has not been obtained by management. A deferred tax valuation allowance of \$4,563,000 offset deferred tax assets at June 30, 2004 based on management's determination that it is more likely than not that such amounts may not be subsequently realized.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(9) Equity**

*New Capital Structure:* Under the new capital structure pursuant to the Company's plan of reorganization, the Company has the authority to issue a total of Twelve Million Five Hundred Thousand (12,500,000) shares of stock, consisting of Two Million Five Hundred Thousand (2,500,000) shares of Preferred Stock, par value \$0.01 per share (the "Preferred Stock") issuable in series ("Series"), and Ten Million (10,000,000) shares of Common Stock, par value \$0.01 per share (the "Common Stock"). Of the Preferred Stock, One Million Two Hundred Fifty Thousand (1,250,000) shares are designated and known as Series A Preferred Stock (the "Series A Preferred Stock") and Five Hundred Thousand Fifty (500,050) shares are designated and known as Series B Preferred Stock (the "Series B Preferred Stock"). The remaining shares of Preferred Stock may be issued from time to time in one or more Series. The Board of Directors is expressly authorized to provide for the issue of all or any of the remaining unissued and undesignated shares of the Preferred Stock in one or more Series, and to fix the number of shares and to determine or alter for each such Series, such powers, designations, preferences, and relative rights and limitations thereof, as shall be stated and expressed in the resolution or resolutions adopted by the Board of Directors providing for the issuance of such shares and as may be permitted by the General Corporation Law of the State of Delaware.

*Issuance of Preferred Stock.* The Company issued 1,071,636 shares of Series A Preferred Stock and 500,042 shares of Series B Preferred Stock to the stockholders of C/M Holdings, Inc. pursuant to the Merger. The preferences, rights and voting powers (and the qualifications, limitations, or restrictions thereof) of the Series A Preferred Stock, the Series B Preferred Stock are as follows:

*Dividends.* Holders of the Series A Preferred Stock and Series B Preferred Stock are each entitled to receive an annual cumulative cash dividend of \$0.25 per share, payable quarterly in arrears. Dividends on the Series A Preferred Stock and the Series B Preferred Stock will commence to accrue as of the Closing Date. The holders of Common Stock are entitled to receive such dividends, payable in cash or otherwise, as may be declared thereon by the Board of Directors from time to time out of assets or funds of the Company that are legally available therefore; provided, that no dividends shall be declared or paid on the Common Stock if accrued dividends on the Series A Preferred Stock or Series B Preferred Stock, as the case may be, have not been paid. The Company currently does not anticipate declaring and paying any cash dividends on the Common Stock.

*Redemption.* The Company is required to redeem, on a pro rata basis, 100,000 shares of Series A Preferred Stock on April 30, 2005, and on each anniversary date thereafter until April 30, 2010, when the Company is required to redeem the balance of the shares of Series A Preferred Stock then outstanding, at the rate of \$5.00 per share plus all accumulated but unpaid dividends thereon. The Company has the right, but not the obligation, to redeem, on a pro rata basis, the Series B Preferred Stock at any time after April 30, 2009, at the rate of \$5.00 per share plus all accumulated but unpaid dividends thereon.

*Conversion.* The holders of Series A Preferred Stock have no conversion rights. The holders of the Series B Preferred Stock have the right, at any time after the Closing Date, and on or before April 30, 2009, to convert each share of Series B Preferred Stock into such number of shares of Common Stock determined by dividing \$5.00 by the Conversion Price then in effect. The initial Conversion Price will be approximately \$1.4535 per share but is subject to anti-dilutive adjustment. On

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(9) Equity (Continued)**

the Closing Date the holders of Series B Preferred Stock have the right to convert the Series B Preferred Stock into approximately 45% of the issued and outstanding shares of Common Stock.

*Liquidation Preference.* In the event of the liquidation, dissolution or winding up of the Company, either voluntary or involuntary, the assets of the Company available for distribution shall be distributed in the following order of preference: to the holders of Series A Preferred Stock, in an amount per share equal to \$5.00 per share (as such dollar amount may be adjusted for stock splits, combinations, reclassifications and the like with respect to the Series A Preferred Stock) plus all accumulated but unpaid dividends thereon; then to the holders of Series B Preferred Stock, in an amount per share equal to \$5.00 per share (as such dollar amount may be adjusted for stock splits, combinations, reclassifications and the like with respect to the Series B Preferred Stock) plus all accumulated but unpaid dividends thereon; and then to the holders of the Common Stock.

*Voting.* The holders of Series A Preferred Stock have no voting rights except as required by law. Except for the election of the members of the Board of Directors of the Company, the holders of the Series B Preferred Stock are entitled to vote upon all matters upon which holders of the Common Stock have the right to vote and are entitled to the number of votes equal to the largest number of full shares of Common Stock into which such shares of Series B Preferred Stock could be converted, with such voting to be counted together with the Common Stock and not separately as a class except as otherwise provided with respect to the election of directors, as more fully described below. The holders of Common Stock have one vote in respect of each share of Common Stock held by such stockholder for all matters submitted to a vote of stockholders of the Company. Cumulative voting is not permitted. The Board of Directors will consist of seven members. The holders of a plurality of the shares of Series B Preferred Stock, voting as a class, are entitled to elect four members of the Board of Directors and the holders of a plurality of the shares of Common Stock, voting as a class, are entitled to elect three members of the Board of Directors.

*Issuance of Common Stock.* The Company issued 2,079,948 shares of Common Stock to the holders of Class 4 Claims, which, following the Merger, represents approximately 55% of the issued and outstanding shares of Common Stock of the Company, after giving effect to the conversion of all of the Series B Preferred Stock to be issued to the shareholders of CMHI pursuant to the Merger. Of the 2,079,948 shares of Common Stock issued to Company's creditors, 1,278,827 shares of Common Stock are restricted from trading for a two-year period following issuance. The balance of the shares of Common Stock issued are not be subject to any trading restrictions. During Fiscal 2004 the Company received \$255,000 in net proceeds from the exercise of stock options for 249,000 shares granted pursuant to the Company's 2003 Stock Option Plan. The Company also received \$69,087 in net proceeds from the sale of Common Stock to employees pursuant to the 2003 Stock Incentive Plan.

*Treasury Stock.* The Company purchased 25,000 shares of Common Stock from a director for \$40,000 during Fiscal 2004.

**(10) Stock Options**

The predecessor company's stock option plans and related options were cancelled in accordance with the plan of reorganization which was confirmed on May 20, 2002. The Company adopted its 2003 Stock Option Plan ("Stock Option Plan") and 2003 Stock Incentive Plan ("Incentive Plan") effective

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(10) Stock Options (Continued)**

January 1, 2003. Under the Stock Option Plan stock options have been awarded to directors, officers and employees. These stock options vest either immediately or over a period up to two years from the date of grant and expire ten years thereafter. A total of 675,000 shares of common stock were reserved for grant under the Stock Option Plan and 325,000 shares were reserved under the Incentive Plan. In February 2003, the Company granted options covering 455,000 common shares from the Stock Option Plan of which 299,000 shares were immediately exercisable. The grant of the remaining options covering 156,000 common shares were contingent upon the Company achieving earnings before taxes, interest, depreciation and amortization ("EBITDA") of \$500,000 for the fiscal year ended June 30, 2003 which the Company achieved. 84,000 of these options vested on June 30, 2004 and 42,000 of these options will vest on June 30, 2005. 30,000 options granted pursuant to achieving the EBITDA requirement were cancelled in April 2004. The Company recognized \$4,900 and \$9,400 for the year ended June 30, 2004 and the ten months ended June 30, 2003, respectively of compensation expense for options granted during the ten months ended June 30, 2003. The Incentive Plan provides an opportunity to employees of the Company to purchase common shares directly from the Company through payroll deductions. As of June 30, 2004, 40,258 shares have been issued under the Incentive Plan.

The following table summarizes the stock option activity of the Reorganized Company from the time it emerged from bankruptcy:

	<u>Options Outstanding</u>		<u>Weighted average remaining contractual life</u>
	<u>Number of Options</u>	<u>Exercise Price</u>	
Outstanding at August 30, 2002 .....	—	—	
Granted .....	455,000	\$1.00	10 years
Exercised .....	—	—	
Forfeited .....	—	—	
Outstanding at June 30, 2003 .....	455,000	1.00	
Granted .....	30,000	1.60	9.7 years
Exercised .....	249,000	1.02	
Forfeited/Cancelled .....	30,000	1.00	
Outstanding at June 30, 2004 .....	<u>206,000</u>	<u>\$1.09</u>	9.1 years
Exercisable at June 30, 2004 .....	<u>154,000</u>	<u>\$1.08</u>	
Exercisable at June 30, 2003 .....	<u>299,000</u>	<u>\$1.00</u>	

The weighted average fair value of the options granted during 2004 was \$0.78 per common share. The fair value of these options was estimated at the date of grant using the minimum value method with the following assumptions; risk free rate of 4.5%, no dividend yield and weighted average expected lives of 60 months. The minimum value method assumes a 50% volatility in the stock price. The Company's stock has been listed on the Nasdaq OTCBB since August 2004.

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(11) Weighted Average Shares and Net Income Per Common Share**

Net income (loss) per common share is calculated as required by FASB Statement of Financial Accounting Standards No. 128, "Earnings Per Share" ("Statement No. 128"). Statement No. 128 requires dual presentation of basic and diluted earnings per share and a reconciliation between the two amounts. Basic earnings per share excludes dilution, and diluted earnings per share reflects the potential dilution that would occur if securities to issue Common Stock were exercised. In loss periods, dilutive common equivalent shares are excluded as the effect would be antidilutive and in periods prior to August 31, 2002, there were no dilutive securities.

The Company issued 2,079,948 shares of Common Stock upon consummation of the Plan on August 30, 2002 and issued 500,042 shares of Series B Preferred Stock which is convertible at the option of the holders into 1,720,130 shares of the Company's Common Stock.

The reconciliation of basic and diluted weighted average common shares and the reconciliation for the basic and diluted earnings per common share for the reorganized company for the ten month period ended June 30, 2003 following consummation of the Plan and the issuance of the new common and convertible preferred stock pursuant to the Plan is as follows:

<u>For the Ten Months Ended June 30, 2003</u>	<u>Net Loss Allocable to Common Shareholders</u>	<u>Shares</u>	<u>Per Share</u>
Basic and diluted loss per common share . . . . .	\$ (7,000)	2,079,948	\$ —

The reconciliation of basic and diluted weighted average common shares and the reconciliation for the basic and diluted earnings per common share for the reorganized company for the year ended June 30, 2004 is as follows:

<u>For the Year Ended June 30, 2004</u>	<u>Net Income Allocable to Common Shareholders</u>	<u>Shares</u>	<u>Per Share</u>
Basic earnings per common share . . . . .	\$747,000	2,344,206	\$0.32
Assumed conversion of Series B preferred . . . . .	125,000	1,720,130	
Diluted earnings per common share . . .	\$872,000	\$4,064,336	\$0.21

Stock options for the purchase of 455,000 and 206,000 shares of Common Stock for the ten months ended June 30, 2003 and the year ended June 30, 2004, respectively have been excluded from the computation of diluted earnings per share because they are antidilutive.

**(12) Investments**

Investments consist of marketable equity and debt securities and have been categorized as available-for-sale. Unrealized gains and losses for available-for-sale securities are included as accumulated other comprehensive income, a component of shareholders' equity until realized. Realized gains and losses on the sale of securities are based on the specific identification method. The Company continually reviews its investments to determine whether a decline in fair value below the cost basis is other than temporary. If the decline in the fair value is judged to be other than temporary, the cost

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(12) Investments (Continued)**

basis of the security is written down to fair value and the amount of the write-down is included in the consolidated statement of operations.

As of June 30, 2004, the Company's investments consisted of (in thousands):

	Cost	Unrealized Gain (Loss)	Market Value
Stocks .....	\$ 7	\$ (6)	\$ 1
Bonds .....	2,729	287	3,016
Total .....	<u>\$2,736</u>	<u>\$281</u>	<u>\$3,017</u>

**(13) Investment in American IronHorse Motorcycle Company, Inc.**

The Company has invested in \$3,018,000 in American IronHorse Motorcycle Company, Inc. ("American IronHorse") as June 30, 2004. The Company owns 9.7% of the equity of American IronHorse and accounts for this investment as a non current asset on the cost basis. The Company invested an additional \$1,395,000 in American IronHorse common stock, subsequent to June 30, 2004 increasing its ownership to 13.9% of American IronHorse's equity. \$600,000 of the investment is financed by the seller with a promissory note at 5% interest per annum requiring monthly payments of principal and interest of \$21,318 for 30 months beginning August 28, 2004. It is possible the Company may increase its investment in American IronHorse and the accounting for the investment may change as a result of increased investments.

Following is summary unaudited balance sheet information for American IronHorse as of June 30, 2004 and December 31, 2003:

(in thousands)	As of June 30, 2004 (Unaudited)	As of December 31, 2003 (Unaudited)
Current assets .....	\$24,206	\$23,892
Total assets .....	<u>\$28,894</u>	<u>\$29,042</u>
Current liabilities .....	\$15,350	\$19,901
Total liabilities .....	<u>19,024</u>	<u>24,589</u>
Stockholders' equity .....	<u>\$ 9,870</u>	<u>\$ 4,453</u>

**XPONENTIAL, INC.**  
**Notes To Consolidated Financial Statements (Continued)**  
**June 30, 2004**

**(13) Investment in American IronHorse Motorcycle Company, Inc. (Continued)**

Following is a summary of unaudited operating information for the six months ended June 30, 2004 and for the year ended December 31, 2003:

<u>(in thousands)</u>	<u>For the Six Months Ended June 30, 2004</u>	<u>For the Year Ended December 31, 2003</u>
	(Unaudited)	(Unaudited)
Total revenue .....	\$36,985	\$65,019
Net loss .....	\$ (191)	\$ (7,770)

**(14) Commitments and Contingencies**

The Company is obligated under various long-term operating lease agreements for store locations and office space. Total rent expense for all operating leases was approximately \$1,257,000, \$192,000, \$192,000, \$500,000 and \$1,749,000 for the years ended June 30, 2004, the year ended June 30, 2003, the five month period ended June 30, 2002, the two month period ended August 31, 2002, and the year ended February 2, 2002, respectively.

Future minimum lease payments under non-cancelable operating leases as of June 30, 2004 are (in thousands):

2005 .....	1,228
2006 .....	1,009
2007 .....	848
2008 .....	802
2009 .....	473
Thereafter .....	<u>187</u>
Total minimum lease payments .....	<u>\$4,547</u>

The Company is involved in various claims and lawsuits arising in the ordinary course of business. Management is not aware of any claims or lawsuits and, if there were any, in the opinion of management, the resolution of these matters would not have a material adverse effect on the Company's consolidated financial position or results of operations.

**(15) Related Party Transactions**

Sanders Morris Harris, Inc. ("SMH"), a related party, employs Jeffrey A. Cummer and Dwayne A. Moyers as officers of a subsidiary and executes security transactions for the Company. Messrs. Moyers and Cummer are also officers and directors of the Company. Commissions paid to SMH were \$40,927 and \$11,302 for the years ended June 30, 2004 and 2003, respectively.

The Company owned an investment in common stock in SMH totaling approximately \$5.1 million as of June 30, 2003. Substantially all of the common stock was sold in July 2003 on which the Company recognized a gain of \$1,630,000.

## ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

## ITEM 8A. CONTROLS AND PROCEDURES

Under the supervision of, and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, the Company has evaluated its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report as required by Rules 13a-15(b) and 15d-15(b) of the Exchange Act. Based on this evaluation, the Company has concluded that its disclosure controls and procedures were operating effectively as designed. As required, the Company will continue to evaluate the effectiveness of these controls and procedures on a quarterly basis.

There were no changes in the Company's internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during its most recently completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

## PART III

## ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT

### Management

The executive officers and directors of the Company as of June 30, 2004 were as follows:

Name	Age	Title
Dwayne A. Moyers . . . . .	35	Chairman of the Board, Chief Executive Officer, Vice President and Director
Robert W. Schleizer . . . . .	50	Chief Financial Officer, Executive Vice President, Treasurer, Secretary and Director
Roger F. Hogan . . . . .	37	Chief Operating Officer and Vice President of PawnMart
Daniel Peat . . . . .	46	Vice President of Administration of PawnMart
Jeffrey A. Cummer . . . . .	46	Vice President and Director
Carroll Dawson . . . . .	50	Director
James R. Richards . . . . .	59	Director

*Dwayne A. Moyers* was appointed Chief Executive Officer in March 2004, Chairman of the Board in September 2002, Vice President in August 2002 and as a Director in March 2001. He has served as President and as a Director of Xponential Advisors, Inc. since October 2003 and as Executive Vice President, Chairman of the Board and as a Director of PawnMart, Inc. since January 2003. Mr. Moyers has served as Interim President of American IronHorse Motorcycle Company, Inc., a motorcycle manufacturer located in Fort Worth, Texas ("American IronHorse"), since June 2004 and as a director of that company since March 1998. Mr. Moyers served as Vice President, Secretary and Treasurer of C/M Holdings, Inc. from November 1994 until its merger with and into the Company in August 2002, and served as a director of that company from May 1997 until August 2002. He has served as Vice President of Hulen Capital Partners, Inc. (formerly Cummer/Moyers Capital Partners, Inc.) since July 1994. Mr. Moyers has served as Vice President, Cummer/Moyers Division, of Sanders Morris Harris Inc. since October 2000. He also served as Vice President of Cummer/Moyers Securities, Inc.

and Cummer/Moyers Capital Advisors, Inc. from September 1996 and October 1996, respectively, until October 2000. Mr. Moyers is a registered investment advisor agent through SMH Capital Advisors, Inc.

*Robert W. Schleizer* was appointed Executive Vice President, Chief Financial Officer, Treasurer and as a Director in January 2001 and as Secretary in April 2004. Mr. Schleizer has served as Chief Financial Officer, Secretary, Treasurer and as a Director of Xponential Advisors, Inc. since October 2003 and as Executive Vice President, Chief Financial Officer, Secretary and Treasurer and as a Director of PawnMart, Inc. since January 2003. He has also served as Chief Financial Officer and Secretary of American IronHorse effective January 13, 2004. Mr. Schleizer is a partner with Tatum CFO Partners, LLP, a national firm of chief financial officers, and has extensive restructuring experience. He is a Certified Insolvency Recovery Adviser.

*Roger F. Hogan* has served as Chief Operating Officer and Vice President of PawnMart, Inc. since January 2003. Mr. Hogan joined the Company in November 1994 as a store associate, and was promoted to Store Manager in April 1995, to District Manager in August 1995 and to Regional Manager in January 2001.

*Daniel Peat* was appointed Vice President of Administration of PawnMart, Inc. in September 2003. He joined PawnMart, Inc. in September 2001 as Controller. Mr. Peat has over twenty years experience in public and private accounting working with Fortune 500 companies and entrepreneurs. He received a Bachelor of Business Administration degree with a certificate in accounting from Southern Methodist University, Dallas, Texas, in 1980.

*Jeffrey A. Cummer* was appointed Vice President and as a Director in August 2002. Mr. Cummer served as President and a director of C/M Holdings, Inc. from November 1990 until its merger with and into the Company in August 2002. He has served as President of Hulen Capital Partners, Inc. since July 1994. Mr. Cummer has served as President, Cummer/Moyers Division, of Sanders Morris Harris Inc. since October 2000. He also served as President of Cummer/Moyers Securities, Inc. and Cummer/Moyers Capital Advisors, Inc. from September 1996 and October 1996, respectively, until October 2000. Mr. Cummer is a Certified Financial Planner. He is also a registered investment advisor agent through SMH Capital Advisors, Inc.

*Carroll Dawson* was appointed as a Director in November 2002. Mr. Dawson has served as President of AB-CO Markets, Inc., a Blockbuster Video franchisee, since December 1992; as general partner of Dawson Properties, Ltd., which owns real estate and securities investments, since April 1996; and as a director of the Bank of Weatherford in Weatherford, Texas since June 2000.

*James R. Richards* was appointed as a Director in May 2001. Mr. Richards is Managing Director of Texas Business Capital, Inc., a merchant banking firm. Mr. Richards served as Managing Director of Dillon-Gage Securities, Inc., an NASD broker/dealer from 1999 to 2001; and as Managing Director of Corporate Finance, Inc., a private investment banking firm from 1994 to 1999. He is a former certified public accountant, and worked with Deloitte & Touche, Certified Public Accountants, for over ten years.

#### **Section 16(a) Beneficial Ownership Reporting Compliance**

Based on the Company's records, management believes that during Fiscal 2004 all directors, officers and ten percent (10%) or greater beneficial owners timely filed all required Section 16(a) reports, except Jeffrey A. Cummer and Dwayne A. Moyers who were each late filing statements of changes in beneficial ownership for transactions occurring on September 30, 2003, and John R. Boudreau, Roger F. Hogan and Robert W. Schleizer who were each late filing statements of changes in beneficial ownership for transactions occurring on November 24, 2003.

## **Code of Ethics**

The Company has adopted a code of ethics that applies to the Company's principal executive officer, principal financial officer, and principal accounting officer. The Company has posted its code of ethics on its website at [www.xponential.us](http://www.xponential.us).

## **Audit Committee**

The Company has a separately-designated standing audit committee established in accordance with section 3(a)(58)(A) of the Exchange Act. The members of the audit committee are James R. Richards (Chairman) and Carroll Dawson. Each member of the audit committee is "independent" within the meaning of the applicable listing standards of The NASDAQ Stock Market and the rules of the Securities and Exchange Commission. The Board has determined that Mr. Richards is an "audit committee financial expert" and "independent" as defined under the applicable rules of the Securities and Exchange Commission.

## **ITEM 10. EXECUTIVE COMPENSATION**

### **Summary of Executive Compensation**

The following table sets forth the cash and noncash compensation for the fiscal year ended June 30, 2004 ("Fiscal 2004"), June 30, 2003 ("Fiscal 2003"), the twelve months ended June 30, 2002 ("Fiscal 2002"), and the fiscal year ended February 2, 2002 ("Fiscal 2001") of (i) the individuals who served as the Company's Chief Executive Officer during Fiscal 2004 and (ii) the Company's four other most highly compensated executive officers who were serving as executive officers as of the end of Fiscal 2004 and whose total annual salary and bonus exceeded \$100,000 (collectively, the "Named Executive Officers").

# SUMMARY COMPENSATION TABLE

Name and Principal Position	Year *	Annual Compensation(1)		Long-Term Compensation Awards
		Salary (\$)	Bonus (\$)	Securities Underlying Options (#)
Dwayne A. Moyers(2)(3)	2004	78,750	—	—
Chairman of the Board, Chief Executive Officer and Vice President	2003	134,135	—	55,000
	2002	2,000	—	—
	2001	—	—	—
Robert W. Schleizer(4)	2004	274,418	—	—
Chief Financial Officer, Executive Vice President and Treasurer	2003	180,000	150,000	130,000
	2002	245,762	—	—
	2001	270,375	—	—
Roger F. Hogan(5)	2004	110,000	16,400	—
Chief Operating Officer and Vice President of PawnMart	2003	110,000	36,271	25,000
	2002	91,000	—	—
	2001	67,333	24,289	—
Jeffrey A. Cummer(3)(6)	2004	78,501	—	—
Vice President	2003	134,135	—	30,000
	2002	—	—	—
	2001	—	—	—
John R. Boudreau(7)	2004	174,415	—	—
Chairman of the Board, President and Chief Executive Officer	2003	144,000	150,000	130,000
	2002	144,554	—	—
	2001	89,169	—	—

\* On May 24, 2002 the Board of Directors changed the Company's fiscal year end from the Saturday nearest January 31 to June 30. Fiscal 2002 refers to the new fiscal year ended June 30, 2002. The amounts listed for Fiscal 2002 are for twelve months and include the last eight months of Fiscal 2001, resulting in an overlap period of eight months.

- (1) The Named Executive Officers received personal benefits in addition to salary and bonuses, the aggregate amount of which did not exceed the lesser of \$50,000 or 10% of the total of their annual salary and bonus, and is therefore not required to be reported.
- (2) Mr. Moyers was appointed Vice President in August 2002, Chairman of the Board in September 2002 and Chief Executive Officer in April 2004.
- (3) Compensation for 2003 includes salary and a one time investment fee of \$75,000 in connection with the Merger. Mr. Moyers' compensation for 2002 includes directors fees.
- (4) Mr. Schleizer is a partner with Tatum CFO Partners, LLP ("Tatum"), which receives a resource fee equal to 20% of Mr. Schleizer's salary. Tatum received total payments of \$57,242, \$36,000, \$19,407 and \$37,913 in Fiscal 2004, Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively.
- (5) Mr. Hogan joined the Company in November 1994 as a store associate. He was promoted to Store Manager in April 1995, District Manager in August 1995, Regional Manager in January 2001, and to Chief Operating Officer in October 2001.
- (6) Mr. Cummer was appointed Vice President in August 2002.
- (7) Mr. Boudreau was appointed Chairman of the Board, President and Chief Executive Officer in June 2001. He resigned as Chairman in September 2002 and as Chief Executive Officer in April 2004.

### Option Grants to Executives

No stock options were granted to the Named Executive Officers in Fiscal 2004.

### Option Exercises and Values

The following table sets forth the value of exercised options and unexercised options at the end of Fiscal 2004 for the Named Executive Officers:

#### AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND FISCAL YEAR END OPTION VALUES

Name	Shares Acquired on Exercise (#)	Value Realized \$(1)	Number of Securities Underlying Unexercised Options at Fiscal Year End (#) Exercisable/ Unexercisable	Value of Unexercised In-The-Money Options at Fiscal Year End (\$ Exercisable/ Unexercisable(1)
Dwayne A. Moyers . . . . .	—	—	45,000 / 10,000	\$45,000 / \$10,000
Robert W. Schleizer . . . . .	100,000	\$100,000	20,000 / 10,000	\$20,000 / \$10,000
Roger F. Hogan . . . . .	10,000	\$ 10,000	10,000 / 5,000	\$10,000 / \$5,000
Daniel A. Peat . . . . .	10,000	\$ 10,000	10,000 / 5,000	\$10,000 / \$5,000
Jeffrey A. Cummer . . . . .	—	—	20,000 / 10,000	\$20,000 / \$10,000
John R. Boudreau . . . . .	100,000	\$100,000	0 / 0	\$0 / \$0

(1) The fair market value of the underlying Common Stock for purposes of this table was \$1.00 per share at June 30, 2004.

### Compensation of Directors

The Board of Directors meets at least quarterly and non-employee Directors are paid a fee of \$1,000 for attendance at each meeting. In addition, non-employee committee members are paid a fee of \$500 for attendance at each committee meeting. Directors are also reimbursed for their ordinary and necessary expenses incurred in attending meetings of the Board of Directors or a committee thereof.

Non-employee Directors are also eligible for stock option grants under the Company's 2003 Stock Option Plan. The number of shares subject to options, as well as the other terms and conditions of the awards (such as vesting and exercisability schedules and termination provisions) are within the discretion of the Board of Directors and the Compensation Committee. During Fiscal 2004 a total of 30,000 options were granted to non-employee Directors, all with an exercise price of \$1.60 per share.

### Employment Contracts and Termination of Employment and Change-in-Control Arrangements

The Company currently has no employment contracts or termination of employment or change-in-control plans or arrangements in effect with any of the Named Executive Officers.

## ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

### Certain Beneficial Owners

The following table sets forth as of June 30, 2004 certain information with respect to the number of shares of each class of voting securities beneficially owned by each person who is known by

management to beneficially own more than 5% of any class of the Company's outstanding voting securities.

Title of Class	Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership(1)	Percent of Class(2)
Common	<b>Jeffrey A. Cummer</b> ..... 4800 Overton Plaza, Suite 300 Fort Worth, Texas 76109	572,597 shares(3)(4)	24.22%
Common	<b>Dwayne A. Moyers</b> ..... 4800 Overton Plaza, Suite 300 Fort Worth, Texas 76109	418,281 shares(3)(5)	17.51%
Common	<b>Robert W. Schleizer</b> ..... 6400 Atlantic Boulevard, Suite 190 Norcross, Georgia 30071	120,000 shares(8)	5.08%
Common	<b>SMH Capital Advisors, Inc.</b> ..... 4800 Overton Plaza, Suite 300 Fort Worth, Texas 76109	533,497 shares(6)	22.76%
Common	<b>Investors Strategic Partners I, Ltd.</b> ..... 4800 Overton Plaza, Suite 300 Fort Worth, Texas 76109	184,994 shares(7)	7.89%

- (1) Unless otherwise noted, the Company believes that each person named has sole voting and investment power with respect to all shares beneficially owned by such persons.
- (2) Based on 2,344,206 shares of Common Stock issued and outstanding on June 30, 2004, as adjusted for the conversion of shares of Series B Preferred Stock into shares of Common Stock and the exercise of options exercisable within sixty days from June 30, 2004 for a specific stockholder pursuant to Rule 13d-3(d)(1) under the Exchange Act.
- (3) Does not include 533,497 shares of Common Stock owned by various investors for which voting and dispositive power in certain cases is held by SMH Capital Advisors, Inc., of which Mr. Cummer and Mr. Moyers are officers and directors.
- (4) Represents 15,257 shares of Common Stock owned directly, 352,346 shares of Common Stock issuable upon conversion of 102,427 shares of Series B Preferred Stock owned directly, 20,000 shares of Common Stock which Mr. Cummer has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan, and 184,994 shares of Common Stock issuable upon conversion of 53,778 shares of Series B Preferred Stock owned by Investors Strategic Partners I, Ltd., a Texas limited partnership ("ISP"), of which Hulen Capital Partners, Inc., a Texas corporation ("HCP"), is the general partner. Mr. Cummer is an officer, director and shareholder of HCP and shares voting and investment power with Mr. Moyers with respect to the shares owned by ISP.
- (5) Represents 15,257 shares of Common Stock owned directly, 173,030 shares of Common Stock issuable upon conversion of 50,300 shares of Series B Preferred Stock owned directly, 45,000 shares of Common Stock which Mr. Moyers has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan, and 184,994 shares of Common Stock issuable upon conversion of 53,788 shares of Series B Preferred Stock owned by ISP. Mr. Moyers is an officer, director and shareholder of HCP, the general partner of ISP, and shares voting and investment power with Mr. Cummer with respect to the shares owned by ISP.

- (6) These shares are owned by various investors for which voting and dispositive power in certain cases is held by SMH Capital Advisors Inc.
- (7) Represents 184,994 shares of Common Stock issuable upon conversion of 53,778 shares of Series B Preferred Stock.
- (8) Represents 75,000 shares of Common Stock owned directly, 15,000 shares of Common Stock which Mr. Schleizer has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan, 25,000 shares of Common Stock owned by Tatum CFO Partners, LLP ("Tatum") and 5,000 shares of Common Stock which Tatum has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to it under the 2003 Stock Option Plan. Mr. Schleizer is a limited partner of Tatum.

## Management

The following table sets forth as of June 30, 2004 certain information with respect to the number of shares of each class of equity securities beneficially owned by all directors and certain executive officers of the Company, individually, and by all of directors and executive officers of the Company as a group.

Title of Class	Name of Beneficial Owner	Amount and Nature of Beneficial Ownership(1)	Percent of Class(2)
Common	Robert W. Schleizer .....	120,000 shares(3)	5.08%
Common	Jeffrey A. Cummer .....	572,597 shares(4)(5)	24.22%
Series A Preferred	Jeffrey A. Cummer .....	334,770 shares(6)	31.24%
Common	Dwayne A. Moyers .....	418,281 shares(4)(7)	17.51%
Series A Preferred	Dwayne A. Moyers .....	223,055 shares(8)	20.81%
Common	James R. Richards .....	35,000 shares(9)	1.47%
Common	Roger F. Hogan .....	20,000 shares(10)	*
Common	Daniel Peat .....	20,000 shares(11)	*
Common	Carroll Dawson .....	19,274 shares(12)	*
Series A Preferred	Carroll Dawson .....	5,778 shares(13)	*
Common	All directors and executive officers as a group (7 persons) .....	1,020,158 shares(14)	40.90%
Series A Preferred	All directors and executive officers as a group (7 persons) .....	448,350 shares(15)	41.84%

\* Less than 1% of the outstanding shares of the class.

- (1) Unless otherwise noted, the Company believes that each person named has sole voting and investment power with respect to all shares beneficially owned by such persons.
- (2) Based on 2,344,206 shares of Common Stock issued and outstanding on June 30, 2004, as adjusted for the conversion of shares of Series B Preferred Stock into shares of Common Stock and the exercise of options exercisable within sixty days from June 30, 2004 for a specific stockholder pursuant to Rule 13d-3(d)(1) under the Exchange Act; and based on 1,071,636 shares of Series A Preferred Stock issued and outstanding on June 30, 2004. The shares of Series A Preferred Stock are not convertible and have no voting rights except as required by law.
- (3) Represents 75,000 shares of Common Stock owned directly, 15,000 shares of Common Stock which Mr. Schleizer has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan, 25,000 shares of Common Stock owned by Tatum CFO Partners, LLP ("Tatum") and 5,000 shares of Common Stock which Tatum has the

right to acquire within sixty days from June 30, 2004 pursuant to options granted to it under the 2003 Stock Option Plan. Mr. Schleizer is a limited partner of Tatum.

- (4) Does not include 533,497 shares of Common Stock owned by various investors for which voting and dispositive power in certain cases is held by SMH Capital Advisors, Inc., of which Mr. Cummer and Mr. Moyers are officers and directors.
- (5) Represents 15,257 shares of Common Stock owned directly, 352,346 shares of Common Stock issuable upon conversion of 102,427 shares of Series B Preferred Stock owned directly, 20,000 shares of Common Stock which Mr. Cummer has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan, and 184,994 shares of Common Stock issuable upon conversion of 53,788 shares of Series B Preferred owned by ISP, of which HCP is the general partner. Mr. Cummer is an officer, director and shareholder of HCP and shares voting and investment power with Mr. Moyers with respect to the shares owned by ISP.
- (6) Represents 219,517 shares of Series A Preferred Stock owned directly and 115,253 shares of Series A Preferred Stock owned by ISP that are beneficially owned by both Mr. Cummer and Mr. Moyers.
- (7) Represents 15,257 shares of Common Stock owned directly, 173,030 shares of Common Stock issuable upon conversion of 50,300 shares of Series B Preferred Stock owned directly, 45,000 shares of Common Stock which Mr. Moyers has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan, and 184,994 shares of Common Stock issuable upon conversion of 53,778 shares of Series B Preferred Stock owned by ISP. Mr. Moyers is an officer, director and shareholder of HCP, the general partner of ISP, and shares voting and investment power with Mr. Cummer with respect to the shares owned by ISP.
- (8) Represents 107,802 shares of Series A Preferred Stock owned directly and 115,253 shares of Series A Preferred Stock owned by ISP that are beneficially owned by both Mr. Cummer and Mr. Moyers.
- (9) Represents 35,000 shares of Common Stock which Mr. Richards has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan.
- (10) Represents 10,000 shares of Common Stock owned directly and 10,000 shares of Common Stock which Mr. Hogan has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan.
- (11) Represents 10,000 shares of Common Stock owned directly and 10,000 shares of Common Stock which Mr. Peat has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan.
- (12) Represents 9,274 shares of Common Stock issuable upon conversion of 2,696 shares of Series B Preferred Stock owned by Dawson Properties, Ltd., a Texas limited partnership ("Dawson Properties") of which Mr. Dawson is general partner, and 10,000 shares of Common Stock which Mr. Dawson has the right to acquire within sixty days from June 30, 2004 pursuant to options granted to him under the 2003 Stock Option Plan.
- (13) Represents 5,778 shares of Series A Preferred Stock owned by Dawson Properties, of which Mr. Dawson is general partner.
- (14) Represents 150,514 shares of Common Stock owned directly by directors and executive officers, 150,000 shares of Common Stock which the directors and executive officers have the right to

acquire within sixty days from June 30, 2004 pursuant to options granted to them under the 2003 Stock Option Plan, 534,650 shares of Common Stock issuable upon conversion of 155,423 shares of Series B Preferred Stock owned directly by directors and executive officers, and 184,994 shares of Common Stock issuable upon conversion of 53,778 shares of Series B Preferred Stock owned by ISP that are beneficially owned by Mr. Cummer and Mr. Moyers.

- (15) Represents 333,097 shares of Series A Preferred Stock owned directly by directors and executive officers, and 115,253 shares of Series A Preferred Stock owned by ISP that are beneficially owned by Mr. Cummer and Mr. Moyers.

## ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The Company was not a party to any transactions or series of transactions in amounts exceeding \$60,000 with directors, nominees for directors, executive officers, security holders discussed under *"Item 11. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters,"* or a member of the immediate family of any of the foregoing, during the last two years, other than the following:

Effective August 30, 2002, C/M Holdings, Inc., a Texas corporation ("CMHI"), an affiliate of Jeffrey A. Cummer and Dwayne A. Moyers, directors and officers of the Company, was merged with and into the Company (the "Merger"). In connection with the Merger, Mr. Cummer and Mr. Moyers, in addition to securities received on a pro rata basis with other security holders of the classes issued, each received a one-time investment fee of \$75,000 from the Company.

During Fiscal 2001 the Company secured a \$600,000 subordinated credit facility from Hulen Pawn Shop Investors, L.L.C. (the "Hulen Note"), an affiliate of Jeffrey A. Cummer and Dwayne A. Moyers, which loan was approved by the Bankruptcy Court on July 16, 2001. The Hulen Note had a maturity date of December 31, 2002, bore interest at a rate of the prevailing prime rate plus 5%, and was convertible, at the option of the lender, into up to 12% of the Company's Common Stock after reorganization. The Hulen Note was repaid in full in September 2002.

On October 3, 2003 the Company purchased from American IronHorse Motorcycle Company, Inc. ("American IronHorse") a \$1,000,000 principal amount 12% secured subordinated note due September 30, 2004 (the "2003 Note") and a warrant to purchase 100,000 shares of common stock of American IronHorse at \$15.00 per share. In connection with the purchase of such securities, American IronHorse granted to the Company, for a period of thirty days immediately following December 31, 2003, the right to purchase up to 166,666 shares of common stock of American IronHorse at \$6.00 per share (the "Additional Shares"). On January 30, 2004 the Company converted the 2003 Note into common stock of American IronHorse at a rate of one share for each \$6.00 of principal converted, for a total of 166,666 shares. In connection with the Company's purchase of the 2003 Note, the Company received a fee of 5% of the purchase price, or \$50,000, and received an additional \$50,000 fee upon conversion of the 2003 Note.

On December 22, 2003 the Company subscribed for 225,000 shares of common stock of American IronHorse pursuant to a rights offering by American IronHorse at \$6.00 per share (total \$1,350,000). On July 30, 2004 the Company subscribed for an additional 100,000 shares of common stock of American IronHorse pursuant to the rights offering share (total \$600,000).

In December 2003 the Company purchased 17,370 shares of common stock of American IronHorse from a former employee for \$104,220. The Company also purchased 1,800 shares of Series A Preferred Stock and 735 shares of Series B Preferred Stock from the same former employee for \$16,044 and \$11,304, respectively, which the Company subsequently converted into 4,558 shares of common stock of American IronHorse. In December 2003 the Company also purchased a total of \$104,000 in principal amount of American IronHorse notes from a terminated employee and her family

members for \$104,815, which the Company subsequently converted into 10,154 shares of common stock of American IronHorse.

In connection with the Company's investment in American IronHorse, on October 3, 2003 the Company's subsidiary Xponential Advisors, Inc. entered into a management agreement with American IronHorse. For these services, Xponential Advisors, Inc. received a management fee of \$5,700 per week for the services of John R. Boudreau, a former director and officer of the Company, and twenty-five (25) shares of common stock of American IronHorse for each hour worked by Robert W. Schleizer, up to a maximum of 24 hours per week. On April 1, 2004 John R. Boudreau became a full-time employee of American IronHorse and American IronHorse discontinued paying Xponential Advisors, Inc. the weekly fee under the management agreement. Mr. Boudreau subsequently resigned his positions with both companies. Although the management agreement terminated on July 31, 2004, Xponential Advisors, Inc. continues to provide management services to the Company. As of September 22, 2004 Xponential Advisors, Inc. has received a total of 23,000 shares of common stock of American IronHorse as compensation for its management services.

In March 2004 the Company entered into a stock purchase and stock option agreement with a shareholder of American IronHorse to purchase up to 84,000 shares of common stock of American IronHorse for \$6.00 per share, of which all shares have been purchased. On July 28, 2004 the Company entered into a stock purchase agreement with the same shareholder for the purchase of 100,000 shares of common stock of American IronHorse for \$6.00 per share, of which all shares have been purchased.

At September 22, 2004 the Company and its subsidiary Xponential Advisors, Inc. collectively owned 730,748 shares (exclusive of warrants to purchase 100,000 shares of common stock of American IronHorse), or 13.88% of the outstanding common stock of American IronHorse.

In addition to the shares owned by the Company and its subsidiary discussed in the preceding paragraph, at September 22, 2004 directors and officers of the Company, directly and through affiliates, collectively owned 1,253,753 shares (exclusive of warrants to purchase 208,707 shares and options to purchase 29,166 shares of common stock of American IronHorse), or 23.83% of the outstanding common stock of American IronHorse. Dwayne A. Moyers, a director and officer of the Company, is also a director of American IronHorse.

Sanders Morris Harris, Inc., a related party which employs Jeffrey A. Cummer and Dwayne A. Moyers, directors and officers of the Company, executes security transactions for the Company. Commissions earned by Sanders Morris Harris, Inc. were \$11,302 for Fiscal 2003 and \$40,927 for Fiscal 2004.

### **ITEM 13. EXHIBITS AND REPORTS ON FORM 8-K**

#### **(a) Exhibits**

<b>Number</b>	<b>Description</b>
2.1	Agreement and Plan of Merger between PawnMart, Inc. and C/M Holdings, Inc. dated August 1, 2002(1)
3.1	Amended and Restated Certificate of Incorporation of PawnMart, Inc. as filed with the Delaware Secretary of State on August 30, 2002(1)
3.2	Certificate of Amendment to Certificate of Incorporation of PawnMart, Inc.(2)
3.3	Amended and Restated Bylaws of PawnMart, Inc.(3)
3.4	Amendment Number One to Amended and Restated Bylaws of PawnMart, Inc.(2)
10.1	PawnMart, Inc. 2003 Stock Option Plan(4)

Number	Description
10.2	Amendment Number One to PawnMart, Inc. 2003 Stock Option Plan(5)
10.3	PawnMart, Inc. 2003 Stock Incentive Plan(4)
10.4	Amendment Number One to PawnMart, Inc. 2003 Stock Incentive Plan(6)
10.5	PawnMart, Inc. Capital Incentive Program dated January 1, 2003 adopted by the Company's Board of Directors on December 16, 2002(7)
10.6	Amendment Number One to PawnMart, Inc. Capital Incentive Program(6)
10.7	Revolving Credit Agreement Between PawnMart, Inc. and Comerica Bank dated August 30, 2002; Revolving Note in the original principal amount of \$4,500,000 payable by PawnMart, Inc. to Comerica Bank dated August 30, 2002; Security Agreement regarding negotiable collateral granted by PawnMart, Inc. to Comerica Bank dated August 30, 2002; and Security Agreement regarding negotiable collateral granted by C/M Holdings, Inc. to Comerica Bank dated August 30, 2002(8)
10.8	Revolving Credit Agreement Between PawnMart, Inc. and Xponential, Inc. and Comerica Bank dated May 19, 2003 (certain exhibits and schedules to this agreement have been omitted; the Registrant agrees to furnish supplementally to the Commission, upon request, a copy of these exhibits and schedules); Revolving Note in the original principal amount of \$4,500,000 payable by PawnMart, Inc. and Xponential, Inc. to Comerica Bank dated May 19, 2003; Security Agreement regarding negotiable collateral granted by Xponential, Inc. to Comerica Bank dated May 19, 2003; and Security Agreement regarding negotiable collateral granted by PawnMart, Inc. to Comerica Bank dated May 19, 2003(12)
10.9	Loan and Security Agreement between PawnMart, Inc., as borrower, Xponential, Inc., as parent, and FCC, LLC, as lender, dated June 17, 2004 *
21.1	Subsidiaries of Xponential, Inc. *
23.1	Consent of Grant Thornton, LLP *
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934, as amended *
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934, as amended *
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 *
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 *
99.1	Confirmation Order dated May 20, 2002(9)
99.2	Debtor's First Amended Plan of Reorganization dated April 3, 2002(9)
99.3	Debtor's First Amended Disclosure Statement dated April 3, 2002(9)
99.4	Fourth Modification to Debtor's First Amended Plan of Reorganization(10)
99.5	Fifth Modification to Debtor's First Amended Plan of Reorganization(11)

\* Filed herewith.

- (1) Filed as an exhibit to the registrant's Current Report on Form 8-K filed on September 16, 2002 (File No. 1-13939).
- (2) Filed as an exhibit to the registrant's Quarterly Report on Form 10-QSB filed on May 15, 2003 (File No. 1-13939).
- (3) Filed as an exhibit to the registrant's Quarterly Report on Form 10-Q filed on August 20, 2002 (File No. 1-13939).
- (4) Filed as an exhibit to the registrant's Definitive Proxy Statement filed on January 28, 2003 (File No. 1-13939).
- (5) Filed as an exhibit to the registrant's Registration Statement on Form S-8 filed on April 16, 2003 (File No. 333-104575).
- (6) Filed as an exhibit to the registrant's Registration Statement on Form S-8 filed on April 16, 2003 (File No. 333-104576).
- (7) Filed as an exhibit to the registrant's Quarterly Report on Form 10-QSB filed on February 14, 2003 (File No. 1-13919).
- (8) Filed as an exhibit to the registrant's Quarterly Report on Form 10-QSB filed on November 20, 2002 (File No. 1-13919).
- (9) Filed as an exhibit to the registrant's Current Report on Form 8-K filed on June 10, 2002 (File No. 1-13919).
- (10) Filed as an exhibit to the registrant's Current Report on Form 8-K/A filed on June 28, 2002 (File No. 1-13919).
- (11) Filed as an exhibit to the registrant's Current Report on Form 8-K/A filed on August 12, 2002 (File No. 1-13919).
- (12) Filed as an exhibit to the registrant's Annual Report on Form 10-KSB filed on October 14, 2003 (File No. 1-13919).
- (b) **Reports on Form 8-K.** No reports on Form 8-K were filed by the Company during the fourth quarter of the fiscal year ended June 30, 2004.

#### **ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

*Audit Fees.* The aggregate fees billed for professional services rendered by Grant Thornton LLP for both the audit of the Company's financial statements as of and for the fiscal year ended June 30, 2003 and 2004 and the review of the financial statements included in the Company's Quarterly Reports on Form 10-Q and Form 10-QSB for Fiscal 2003 and Fiscal 2004 were \$91,873 in Fiscal 2003 and \$91,535 in Fiscal 2004. These fees were approved by the Audit Committee.

*Audit-Related Fees.* The aggregate fees billed by Grant Thornton LLP for audit-related services were \$0 in Fiscal 2003 and \$738 in Fiscal 2004. These services in Fiscal 2004 consisted of review of the Company's proxy statement and attendance at the 2003 annual shareholders meeting. These were no audit related services billed in Fiscal 2003.

*Tax Fees.* The aggregate fees billed by Grant Thornton LLP for tax services were \$0 in Fiscal 2003 and \$0 in Fiscal 2004. There were no tax services provided by Grant Thornton LLP in Fiscal 2003 or Fiscal 2004.

*All Other Fees.* The aggregate fees billed by Grant Thornton LLP for all other services were \$0 in Fiscal 2003 and \$20,190 in Fiscal 2004. There were no other services provided in Fiscal 2003. These services in Fiscal 2004 consisted of review of the Company's Form SB-2 filed on January 26, 2004.

Under its Charter, the Audit Committee must pre-approve all engagements of the Company's independent auditors unless an exception to such pre-approval exists under the Exchange Act or the rules of the Securities and Exchange Commission. Each year the independent auditors' retention to audit the Company's financial statements, including the associated fee, is approved by the Audit Committee. At the beginning of the fiscal year the Audit Committee will evaluate other known potential engagements of the independent auditors, including the scope of the work proposed to be performed and the proposed fees, and approve or reject each service, taking into account whether the services are permissible under applicable law and the possible impact of each non-audit service on the independent auditors' independence from management. At each subsequent Audit Committee meeting the Audit Committee will receive updates on the services actually provided by the independent auditors and management may present additional services for approval. During Fiscal 2004 each new engagement of Grant Thornton, LLP was approved in advance by the Audit Committee.

## SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

XPONENTIAL, INC.

September 27, 2004

By: /s/ DWAYNE A. MOYERS  
Dwayne A. Moyers  
*Chief Executive Officer and Vice President*

September 27, 2004

By: /s/ ROBERT W. SCHLEIZER  
Robert W. Schleizer  
*Executive Vice President and Chief Financial Officer*

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ DWAYNE A. MOYERS</u> Dwayne A. Moyers	Chairman of the Board, Chief Executive Officer, Vice President and Director	September 27, 2004
<u>/s/ ROBERT W. SCHLEIZER</u> Robert W. Schleizer	Executive Vice President, Chief Financial Officer, Treasurer, Secretary and Director	September 27, 2004
<u>/s/ JEFFREY A. CUMMER</u> Jeffrey A. Cummer	Vice President and Director	September 27, 2004
<u>/s/ J. ROBERT COLLINS</u> J. Robert Collins	Director	September 27, 2004
<u>/s/ CARROLL DAWSON</u> Carroll Dawson	Director	September 27, 2004
<u>/s/ JAMES R. RICHARDS</u> James R. Richards	Director	September 27, 2004

**CERTIFICATION**

I, Dwayne A. Moyers, certify that:

1. I have reviewed this annual report on Form 10-KSB of Xponential, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;
4. The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and
5. The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: September 27, 2004

/s/ DWAYNE A. MOYERS

Dwayne A. Moyers  
Chief Executive Officer

## CERTIFICATION

I, Robert W. Schleizer, certify that:

1. I have reviewed this annual report on Form 10-KSB of Xponential, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;
4. The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and
5. The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: September 27, 2004

/s/ ROBERT W. SCHLEIZER

Robert W. Schleizer  
Chief Financial Officer

**CERTIFICATION**

The undersigned, Dwayne A. Moyers, the Chief Executive Officer of Xponential, Inc. (the "Company"), pursuant to 18 U.S.C. §1350, hereby certifies that:

- (i) the annual report on Form 10-KSB of the Company for the fiscal year ended June 30, 2004 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: September 27, 2004

/s/ DWAYNE A. MOYERS

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Dwayne A. Moyers  
Chief Executive Officer

**CERTIFICATION**

The undersigned, Robert W. Schleizer, the Chief Financial Officer of Xponential, Inc. (the "Company"), pursuant to 18 U.S.C. §1350, hereby certifies that:

- (i) the annual report on Form 10-KSB of the Company for the fiscal year ended June 30, 2004 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: September 27, 2004

/s/ ROBERT W. SCHLEIZER

Robert W. Schleizer  
Chief Financial Officer